الوطني
NBK

Annual Report and Financial Statements 2012

• Safety • Stability • Strength

Contents

HH Sheikh

Sabah Al-Ahmad Al-Jaber Al-Sabah

Emir of the State of Kuwait

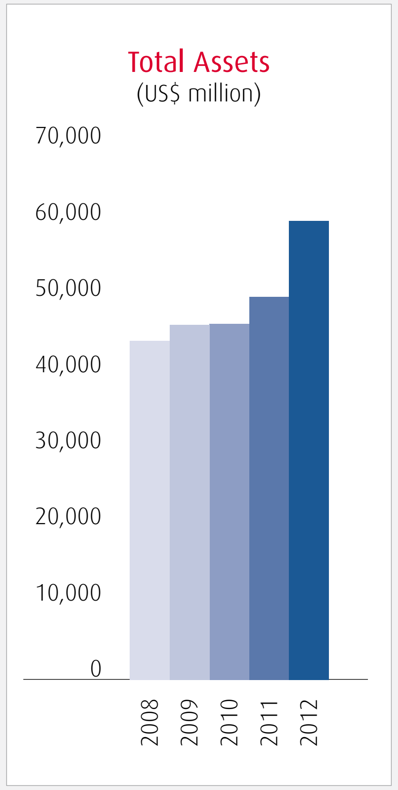
HH Sheikh

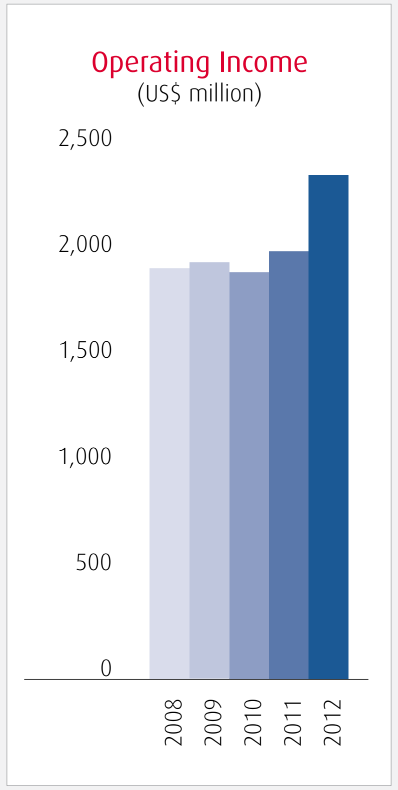
Nawaf Al-Ahmad Al-Jaber Al-Sabah

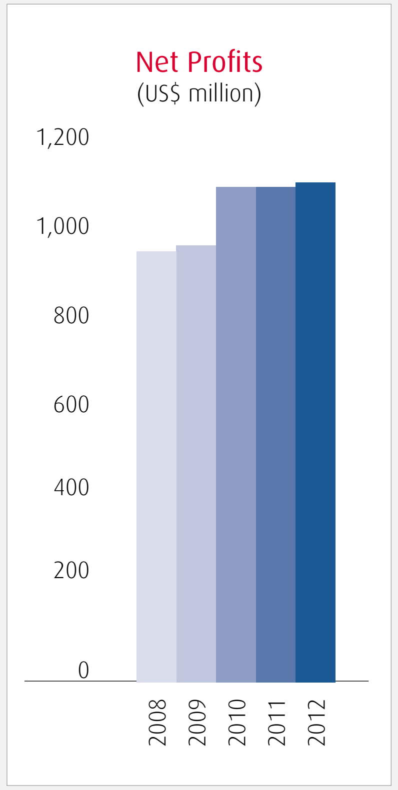
Crown Prince of the State of Kuwait

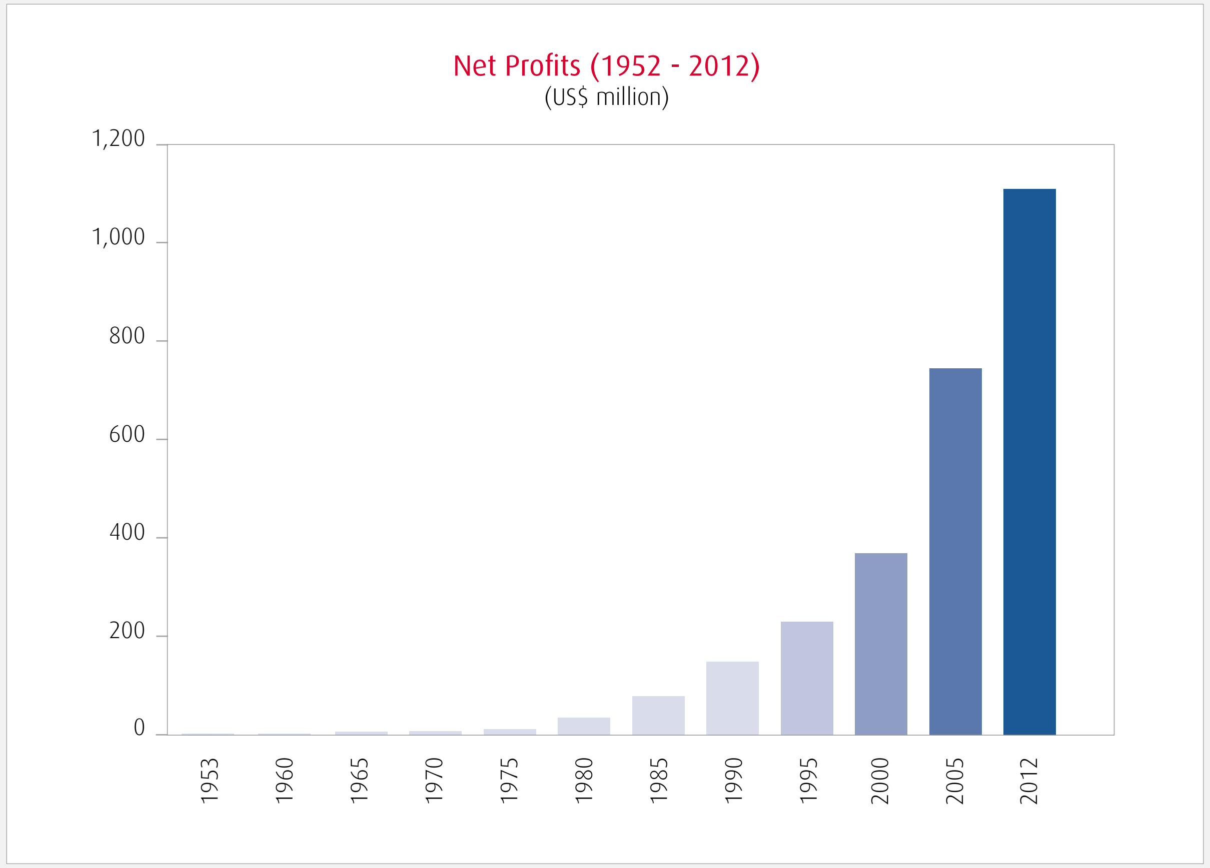
Financial Highlights

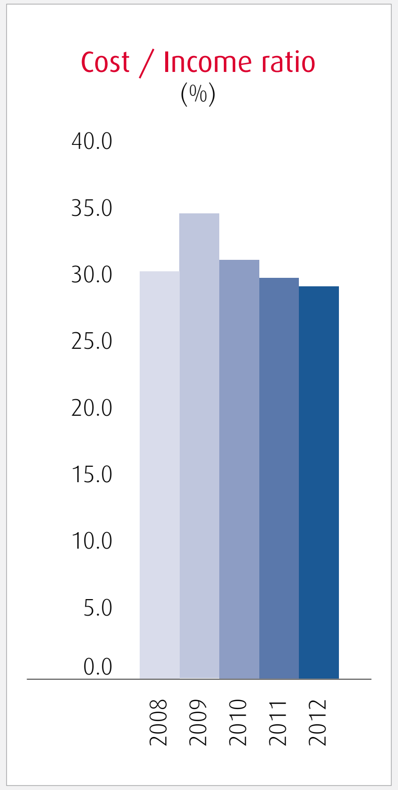
(In US$ millions, except where noted)	2008	2009	2010	2011	2012
Net interest income & Net income from Islamic financing	1,304	1,340	1,276	1,355	1,414
Non-interest income	504	504	497	566	896
Operating expenses	567	640	566	576	653
Net profit	908	943	1,073	1,075	1,085
Total assets	42,572	45,892	45,863	48,451	58,398
Assets under management	10,076	8,590	9,259	8,996	10,016
Shareholder's equity excluding proposed dividend	5,121	6,073	7,375	7,707	8,172
Market capitalization	10,943	11,663	18,369	15,639	14,585
Return on beginning equity excluding proposed dividends %	17.0	18.4	17.7	14.6	14.1
Year-end price per share - US$	4.20	3.98	5.12	3.98	3.41
Basic earnings per share (Cents)	22	23	26	25	25
Proposed cash dividends (Cents)	16	14	14	14	11
Proposed bonus shares (%)	10	10	10	10	5

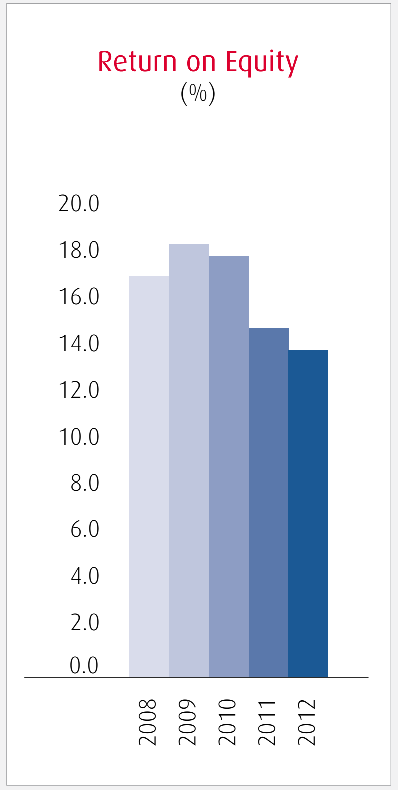


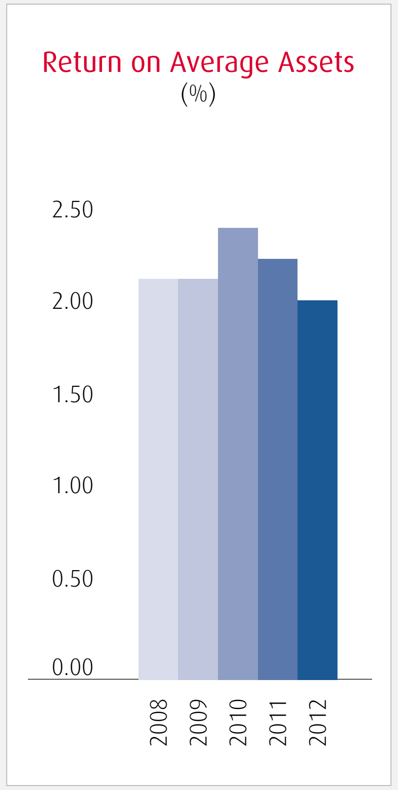












Our Mission

To be the premier Arab Bank

To achieve consistently superior returns
for our shareholders

To deliver world-class products and services
to our customers

To invest in people

To benefit the communities in which we operate

NBK at a glance

NBK was established in 1952 as the first local bank and the first shareholding company in Kuwait and the Gulf region. Over the years, NBK has remained the leading financial institution in Kuwait and has successfully extended its well-established franchise throughout the Middle East. NBK currently operates through a large international network covering the world's leading financial and business centers across 16 countries.

NBK has long been recognized for its excellent and stable management team and its clear and focused strategy. NBK's strength rests on its consistent profitability, high asset quality, and strong capitalization. NBK offers a full spectrum of innovative and unrivalled financial and investment services and solutions for individuals, corporate and institutional clients. NBK currently enjoys a dominant market share with a large and ever expanding local and regional client base.

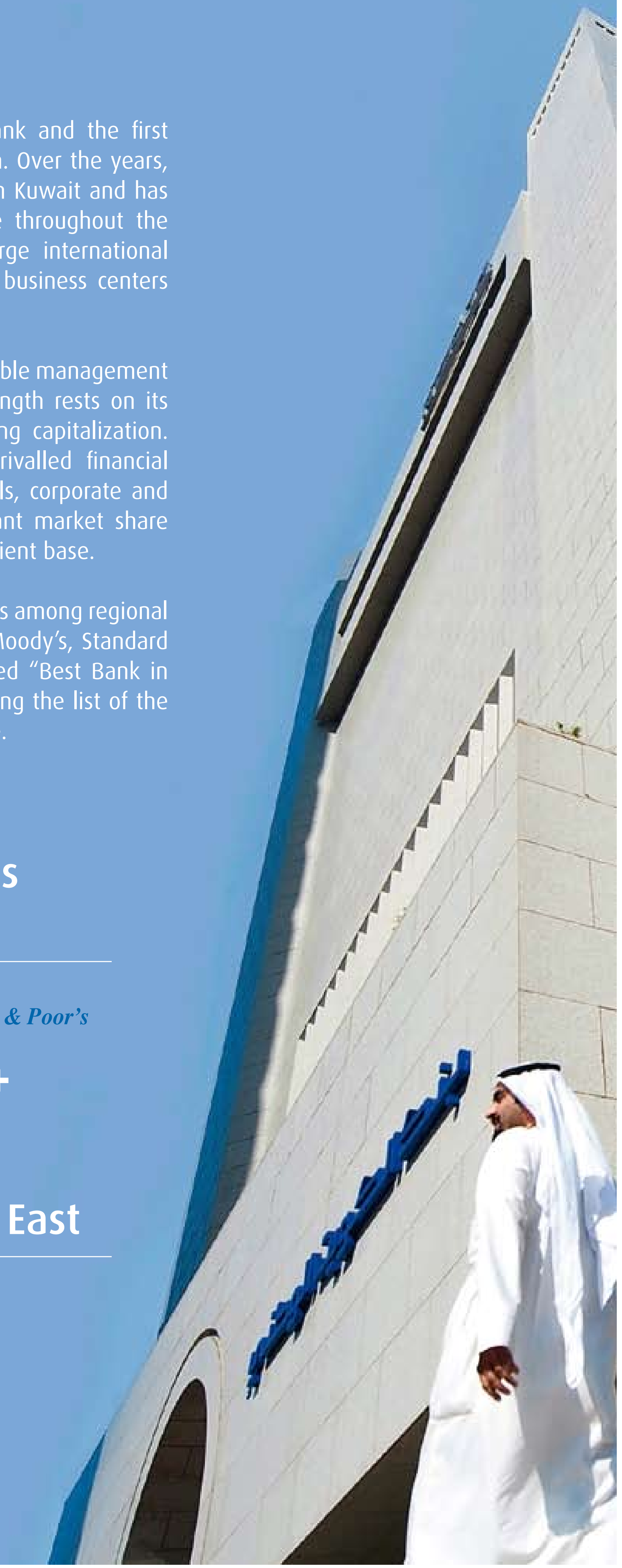
NBK has consistently been awarded the highest ratings among regional banks by the major international ratings agencies; Moody's, Standard & Poor's and Fitch Ratings. In 2012, NBK was named "Best Bank in the Middle East" by Global Finance, and ranked among the list of the world's 50 safest banks for the sixth consecutive time.

Highest Credit Ratings in the Middle East

Moody's	FitchRatings	Standard & Poor's
Aa3	AA-	A+

Best Bank in the Middle East

Global Finance



NBK across the globe

1 **KUWAIT** (No. of branches 64)
Tel: +965 2242 2011
Fax: +965 2259 5804

WATANI FINANCIAL BROKERAGE COMPANY
Tel: +965 2259 5102
Fax: +965 2224 6979

NBK CAPITAL
Tel: +965 2224 6901
Fax: +965 2224 6905

2 **IRAQ** (No. of branches 14)
Credit Bank of Iraq
Tel: +964 1 7182198 / 7191944
Tel: +964 1 718884406 / 7171673
Fax: +964 1 7170156

3 **JORDAN** (No. of branches 4)
Tel: +962 6 580 0400
Fax: +962 6 580 0441

4 **LEBANON** (No. of branches 8)
Tel: +961 1 759 700
Fax: +961 1 747 866

5 **SAUDI ARABIA**
Jeddah Branch
Tel: +966 2 653 8600
Fax: +966 2 653 8653

6 **BAHRAIN** (No. of branches 2)
Tel: +973 17 155 555
Fax: +973 17 104 860

7 **QATAR** (No. of branches 10)
Tel: +974 4447 8000
Fax: +974 4447 3710

8 **UNITED ARAB EMIRATES**
Dubai Branch
Tel: +971 4 2929222
Fax: +971 4 2943337

NBK Capital - UAE
Tel: +971 4 3652800
Fax: +971 4 3652805

9 **EGYPT** (No. of branches 42)
Al Watany Bank of Egypt
Tel: +202 333 88816 / 17
Fax: +202 333 79302

10 **TURKEY** (No. of branches 20)
Turkish Bank
Tel: +90 212373 6373
Fax: +90 212225 0353

11 **SWITZERLAND**
Tel: +41229064343
Fax: +41229064399

12 **FRANCE**
Paris Branch
Tel: +33 1 5659 8600
Fax: +33 1 5959 8623

13 **UNITED KINGDOM**
London Branch
Tel: +44 20 7224 2277
Fax: +44 20 7224 2101

14 **UNITED STATES OF AMERICA**
New York Branch
Tel: +1 212 303 9800
Fax: +1 212 319 8269

15 **CHINA**
Shanghai Representative Office
Tel: +86 21 6888 1092
Fax: +86 21 5047 1011

16 **SINGAPORE**
Singapore Branch
Tel: +65 6222 5348
Fax: +65 6224 5348

NBK maintained its lead in the domestic market where it has a dominant position. It now has 64 branches and over 200 ATMs in Kuwait. The bank strengthened its position in the region, where its expansion is part of a strategy to diversify revenue streams and to achieve growth. NBK made further consolidation of its regional operations, bringing the full benefits of its unrivalled core management and treasury function to extract synergies and enable closer integration. The Bank's international network now comprises 173 branches, subsidiaries and representative offices in 16 countries on four continents, of which 10 are in the Middle East.

Board of Directors

1 **Mohammad Abdul Rahman Al-Bahar**
Chairman

2 **Nasser Musaed Abdullah Al-Sayer**
Vice Chairman

3 **Hamad Abdul Aziz Al-Sager**
Board Member

4 **Ghassan Ahmed Saoud Al-Khalid**
Board Member

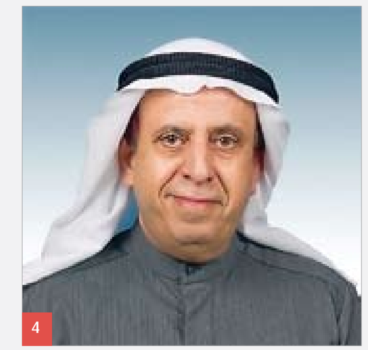
5 **Yacoub Yousef Al-Fulaij**
Board Member

6 **Hamad Mohammed Abdul Rahman Al-Bahar**
Board Member

7 **Muthana Mohamed Ahmed Al-Hamad**
Board Member

8 **Haitham Sulaiman Hamoud Al-Khaled**
Board Member

9 **Loay Jassim Mohammed Al-Kharafi**
Board Member



Chairman's Message 2012

Dear Shareholders,

On behalf of the board members, I am honored to present to you National Bank of Kuwait Group's 60th annual report. As always, NBK proved to be resilient in 2012 withstanding the protracted economic downturn in the developed markets as well as the geopolitical instability in the MENA region.

This is a special year for NBK as in 2012 the bank celebrates its 60th anniversary. NBK was established in 1952 as the first Kuwaiti bank and the first company in the gulf region. Over the past 60 years, the bank has delivered exceptional performance serving the Kuwaiti economy, meeting the needs and expectations of its customers and creating value for its shareholders.

In 2012, we managed to maintain our solid performance, generating strong profits and strengthening our financial position. Also this year, NBK took firm steps in the implementation of its income diversification strategy. This included increasing our stake in Boubyan Bank so that it became a subsidiary and growing the contribution of the international banking division to overall group profits.

Sixty Years of Serving Kuwait

Since its inception, NBK Group has continuously delivered success on all fronts. In addition to its significant role in the development and progress of Kuwait, NBK grew from a small local banking boutique to one of the largest financial institutions in the region, with operations in 16 countries covering four continents. Today, NBK Group carries the highest credit ratings in the Middle East and North African region from all rating agencies and is recognized among the fifty safest banks in the world by international financial publications.

In each of those sixty years, NBK was steadily maximizing value for its shareholders and growing the return on their investment while maintaining solid profits even through several local, regional and international crises that radically altered the landscape of the global banking industry. Even so, NBK was able to grow shareholders' equity from just one million Kuwaiti dinars in 1952 to KD 2.3 billion as of December 2012.

Strong Financial Performance

NBK Group delivered a strong set of results in 2012 notwithstanding the challenging operating environment and protracted consequences of the instability in global markets. Locally, business sentiment remained negative as government spending continued to fall behind schedule. The operating environment in Kuwait stalled leading to an underperforming stock market. Consequently asset values came under pressure. Internationally, the global financial crisis continued to set the scene for global demand, while the ongoing Europe's debt concerns create further uncertainty and mixed outlooks. Moreover, the region witnessed significant geopolitical developments that had repercussions on the rest of the region and added to the uncertainty for political and economic prospects.

Despite this, NBK Group performed strongly thanks to the bank's resilience, clear strategy, conservative culture, high professional standards and stable management team, all of which have limited the bank's exposure to lower quality assets in and outside of Kuwait.

NBK achieved net profits of KWD 305.1 million in 2012, which contributed more than 50% of the profits of the Kuwaiti banking sector for the year and confirmed NBK's lead position in Kuwait. High returns to our shareholders remained the focus of the group. Return on equity and return on assets were strong by regional and international standards reaching 14.1% and 2.0%, respectively. As capital ratios become more important in such gloomy times, NBK's capital adequacy ratio reached a comforting 17.0% at year-end 2012 ahead of most peers and significantly above all regulatory requirements.

As of the end of December 2012, total group assets reached KWD 16.4 billion and total shareholders' equity grew to KWD 2.3 billion.

NBK Board of Directors has recommended the distribution of 30 fils cash dividend per share, representing 30% of the nominal share value. The board has also recommended the distribution of a 5% bonus share (5 shares for every 100 shares owned) to shareholders registered at the time of the Annual General Assembly.

Highest Rated in The Middle East

Around the world, NBK is recognized as the premier Arab bank. Its strong reputation is well founded: NBK continues to hold the highest credit ratings among banks in the Middle East, with rating agencies confirming the bank's leading franchise, strong financial position, robust asset quality and above peers earnings generation capabilities. NBK has also been recognized for its clear and consistent strategic direction, its transparency and strong governance and the stability and professionalism of its management team.

Despite the recent downgrades of major Banks and Financial Institutions internationally, NBK maintained the highest ratings among its peers. NBK is rated "Aa3" by Moody's, "AA-" by Fitch Ratings and carries a "A+" rating from Standard and Poor's. All ratings have a stable outlook.

Recognition from rating agencies is especially important in times of volatility and turmoil as credit ratings become fundamental for assessing a financial institution's quality. They further confirm NBK's solid reputation and regional leadership. Added to this, NBK has maintained its standing in the "Global Finance" list of the 50 Safest Banks in the World for the sixth consecutive time, ahead of the most prominent banks internationally.

Regional Expansion Strategy Pays Off

NBK Group's regional expansion strategy has been validated by the Arab world's changing geopolitical realities. Despite unrest and a challenging operating environment, NBK's regional operations proved resilient.

NBK remains committed to its strategy of balancing its revenues in Kuwait and outside, with its international banking profits recorded a year-on-year growth of 22.7% in 2012. The bank is also keen on strengthening its presence where there are growth prospects in the GCC, especially in Qatar through our associate, International Bank of Qatar (IBQ). This is also the case in Saudi Arabia and the United Arab Emirates, both of which have positive economic prospects because of mega infrastructure projects and high capital spending. In that context, NBK received regulatory approvals last year to open a branch in Abu Dhabi to enhance its presence in the UAE.

At the same time, we remain committed to Egypt as a long term strategic market. Despite the current political turmoil we believe in the long term prospects for the Egyptian economy and the potential opportunities in the region's largest market. We've also witnessed solid growth in Egypt. We have experienced only limited impact to our operations there thanks to our conservative and consistent strategy and determination to remain forward-thinking by building a professional class of talent imbued with NBK values, culture and professionalism as groundwork for the future.

Islamic Banking

NBK increased its stake in Boubyan Bank to 58.4% in 2012, which enhanced our presence in the growing market of Islamic banking. With that acquisition of a strategic stake, Boubyan Bank became a subsidiary, with potential for significant improvement in profitability and market share. NBK will continue supporting Boubyan Bank by providing world class talent and expertise though we remain committed to operating as two separate entities.

Governance

Success is built and NBK's success is built on a solid foundation of rigorous and independent risk management practices, a conservative strategy, stable leadership and sound corporate governance systems and principles. Our long serving board and executive management team have taken the lead in implementing and enforcing strict risk management policies ring-fenced from outside interference and in full compliance with all policies and regulations promulgated by government authorities.

NBK has been recognized for the last three consecutive years for the best practices of its Investor Relations function which demonstrate the bank's dedication to transparency and high level of disclosure.

Our International Advisory Board provides a critical sounding board for bank strategy and for understanding the changes taking place within the global financial system. Being the first Arab bank to have an international advisory board, NBK benefits from the expertise, experience and first-hand knowledge of a diverse group of some of the world's most prominent and respected business, financial and political leaders.

Human Resources and CSR

NBK remains highly committed to Kuwait's society and community. We believe that our people are our most valuable resource and to that end we've implemented numerous professional training programs to continue developing our employees while focusing our recruitment efforts on hiring and training the country's best and brightest minds.

In 2012, NBK secured more than 3,615 training opportunity for its employees across various divisions of the bank. We continued working with our training partners as we focus on grooming our next generation of leaders and providing a forum for them to acquire best practices in management, leadership and strategic thinking. Supporting the government's Kuwaitization initiative, NBK Group hired 303 nationals, with nationals now comprising at least 60 percent of the Group's employees. We also extended our initiatives to our international operations. Several trainings were initiated in most of our regional operations to raise technical levels and the standards of working practices.

NBK's commitment to corporate social responsibility is evident in the numerous cultural, community and social activities and charities the bank supported throughout the year. Among the most important initiatives is the bank's donation of KWD2 million to establish a specialized center for the treatment of leukemia in children in the National Bank of Kuwait Hospital for Children.

Additionally, NBK organized a series of community and health initiatives, including a widely popular walkathon aimed at encouraging a healthier lifestyle for people in Kuwait. Our Ramadan social program included providing iftar for hundreds in Kuwait daily while we continued our commitment and support of several activities aimed at protecting and preserving the environment.

Thanks and Appreciation

Finally, on behalf of the board and executive management of the bank, I would like to thank the authorities and regulators for their ongoing support of Kuwait's economic stability and growth. We would also like to express our deepest appreciation and thanks to the Central Bank of Kuwait for its continued support and leadership and its steady guidance during a very challenging year.

We thank our shareholders and our customers for the trust they place in us and for their continued support of NBK as the top financial institution in Kuwait and one of the leading banks in the MENA region.

I would like to thank our Group Chief Executive Officer for his incisive leadership and our executive and management teams and our devoted employees for their commitment and professionalism. It has always been the people behind the bank that have led the way forward and I am confident of a bright and profitable future. I am confident in NBK's strategy, its leadership and its way forward and am honored to chair the world's premier Arab bank.

Mohammed Abdul Rahman Al-Bahar
Chairman of the Board of Directors

International Advisory Board

Chairman:

1 **Sir John Major**
Former Prime Minister of the United Kingdom

Members:

2 **HRH Prince Turki Al-Faisal**
Chairman, King Faisal Centre for Research and Islamic Studies, Saudi Arabia

3 **Josef Ackermann**
Chairman, Zurich Insurance Group Ltd, Switzerland

4 **Abdlatif Al-Hamad**
Chairman and Director General, Arab Fund for Economic and Social Development, Kuwait

5 **Mukesh Ambani**
Chairman and Managing Director, Reliance Industries Limited, India

6 **Anthony Cordesman**
Arleigh A. Burke Chair in Strategy, CSIS, US

7 **Charles H. Dallara**
Managing Director, Institute of International Finance, US

8 **Tom De Swaan**
Chairman, Van Lanschot Bankiers, Netherlands

9 **Suzan Sabancı Dinçer**
Chairman and Executive Board Member, Akbank, Turkey

10 **Mohamed El-Erian**
CEO and co-CIO, PIMCO, US

11 **Martin Feldstein**
President Emeritus of NBER and Professor of Economics, Harvard University, US

12 **Goh Chok Tong**
Emeritus Senior Minister and Senior Advisor, Monetary Authority of Singapore

13 **Steve H. Hanke**
Professor of Applied Economics, Johns Hopkins University, US

14 **Cees Maas**
Senior Advisor Cerberus Global Investment Advisors, Honorary Vice-Chairman and former CFO ING Group, Netherlands

15 **Edward Morse**
Managing Director, Global Head of Commodity Research, Citigroup, US

16 **Lubna Olayan**
Deputy Chairman and CEO, Olayan Financing Company, Saudi Arabia

17 **William Rhodes**
Senior Advisor and Former Senior Vice Chairman, Citigroup, US

18 **Naguib Sawiris**
Chairman and CEO, Orascom Telecom Holding S.A.E., Egypt

19 **Klaus Schwab**
Founder and Executive Chairman, World Economic Forum, Switzerland

Executive Management

1 **Ibrahim S. Dabdoub**
Group Chief Executive Officer

2 **Isam J. Al-Sager**
Deputy Group Chief Executive Officer

3 **Shaikha K. Al-Bahar**
Chief Executive Officer for Kuwait

4 **Salah Y. Al-Fulaij**
CEO- NBK Capital

5 **Omar Bouhadiba**
Acting General Manager
International Banking Group

6 **Mazin Al-Nahedh**
Group General Manager
Consumer Banking Group

7 **Georges Richani**
Group Chief Investment Officer
and Treasurer

8 **Jim Murphy**
Group Chief Financial Officer

9 **Parkson Cheong**
Group Chief Risk Officer

10 **Dr. Soliman Abdel-Meguid**
General Councel
Head Legal Affairs Group

11 **Dr. Randa Azar-Khoury**
Group Chief Economist
Economic Research

12 **Pradeep Handa**
General Manager Foreign Corporate,
Oil & Trade Finance Group

13 **Tony J. Daher**
General Manager - Corporate Banking Group

14 **Malek J. Khalife**
General Manager - Private Banking Group

15 **Andre Loots**
General Manager - Operations Group

16 **Adel Hechme**
General Manager - Human Resources

17 **Carl Ainger**
Group Chief Internal Auditor

Serving Kuwait for 60 Years

Special NBK 60th Anniversary Edition (1952 - 2012)

This past year was a double celebration. Kuwait was marking the 50th anniversary of the promulgation of its constitution. And the National Bank of Kuwait celebrated its sixtieth anniversary. The bank that started operations in a very modest building is now one of the biggest banking institutions in the Arab world as well as one of the safest banks in the world. NBK remains the top rated bank in the Middle East by all international credit rating agencies.

H.H. The Emir attending a presentation on NBK's history.

H.H. The Emir signs the commemorative registry of NBK's sixtieth anniversary.

H.H. The Emir and H.H. The Crown Prince with NBK's Board of Directors and Management team.

The National Bank of Kuwait celebrated its sixty successful years with a grand reception attended by his highness the Emir of Kuwait Sheikh Sabah Al-Ahmed Al-Jaber Al-Sabah and Crown Prince Sheikh Nawaf Al-Ahmed Al-Jaber Al-Sabah as well as other leading Kuwaiti personalities.

NBK has been present through every phase of Kuwait's economic development and has expanded through the setting up of branches and subsidiaries across the region. NBK has gone from strength to strength over the past 60 years to become one of the most prestigious and successful banks in the region with a well-earned reputation for reliability and trustworthiness.

Need for a National Bank...

Kuwait gained its independence as a sovereign state at the end of 1961. However, the state had gained its financial independence with the establishment of the National Bank of Kuwait in 1952. It was the first local bank and the first company capitalized by shareholders in the Gulf, with a start-up capital equivalent to one million

Kuwait in the 1950s.

Kuwaiti dinars and under the name "The National Bank of Kuwait LTD".

The story of NBK began when a group of leading Kuwaiti merchants identified the need to set up a bank to serve the national interest, to contribute to economic growth and to take good care of customer deposits. In early 1952, members of the leading Kuwait merchant families who conceived of setting up the bank met the then Emir, Sheikh Abdullah Al-Salem Al-Sabah. They were:

1- Khalid Al-Zaid Al-Khalid
2- Ahmed Al-Saud Al-Khalid
3- Khalid Abdullatif Al-Hamad
4- Khalifa Al-Khalid A-Ghunaim
5- Sayed Ali Sayed Suleiman Al-Rifai
6- Abdulaziz Al-Hamad Al-Sager
7- Mohamed Abdulmohsen Al-Khurafi
8- Yousef Ahmed Al-Ghanim
9- Yousef Abdulaziz Al-Fulaij

On 19 May 1952 the Emir issued a decree setting up the National Bank of Kuwait. On 15 November 1952, NBK was officially inaugurated as a joint-stock company with a mission to carry out standard banking activities. It was the birth of the first national bank and the first shareholding company in Kuwait and the Gulf.

Weathering Crises...

NBK's glorious success and dazzling achievements started years after its establishment with an Arab executive team taking control of the bank's management. Previously and in its early years, NBK was recognized as "a sleeping giant" as described by international consultancy firms at the time. The new management team proved successful at all fronts, facing various crises unscathed and putting the bank on the path of regional growth.

The early 1980s posed very serious challenges to the banking system in Kuwait and NBK proved its worth. In the collapse of the banking system in 1982 triggered by the Souq Al-Manakh crisis, NBK alone was able to weather the storm thanks to its responsible, balanced and conservative attitude towards risk.

NBK
الوطني

بسم الله الرحمن الرحيم

حضرة صاحب السمو

الشيخ صباح الأحمد الجابر الصباح

أمير البلاد المفدّى حفظه الله ورعاه

إنه لمن دواعي سرورنا رعاية وحضور حفل الإحتفال بذكرى مرور ستين عاماً على تأسيس بنك الكويت الوطني .

تأتي هذه الذكرى تتويجاً لمسيرة النجاح الذي حققه بنك الكويت الوطني منذ إنطلاقته قبل ستين عاماً من بنك محلي صغير إلى أن أصبح في عداد المصارف الكبرى على المستوى المحلي والدولي من خلال مواصلة تطوره ونجاحاته ، مستذكرين بهذه المناسبة أولئك الرجال من الرعيل الأول اللذين أخذوا على عاتقهم تأسيس بنك وطني يلبي إحتياجات الوطن ، ويسهم في تطوير وتنمية الإقتصاد الوطني والمشاركة في بنائه ، وتنمية مدخرات المودعين .

كما نشيد أيضاً بما يقوم به بنك الكويت الوطني من دور بارز في الارتقاء بالخدمات المصرفية في وطننا العزيز .

ننتهز هذه المناسبة للإعراب عن خالص تهانينا للإخوة رئيس وأعضاء مجلس إدارة البنك ، وكافة العاملين فيه ، ومتمنين للجميع دوام التوفيق والنجاح .

صباح الأحمد الجابر الصباح

أمير دولة الكويت

الكويت في : ٩ رجب ١٤٣٣ هـ

الموافق : ٣٠ مايو ٢٠١٢ م

30 مايو 2012

بمناسبة مرور 60 عاماً على تأسيس بنك الكويت الوطني

H.H. The Emir's speech in NBK's sixtieth anniversary ceremony.

The Journey Begins...

NBK quickly showed its professionalism and capability in its contribution to the development of Kuwait. NBK provided the complete range of services to private customers and corporate clients alike. It financed infrastructure projects that began in the 1950s as the nascent state moves into a new era of freedom and economic independence.

Currency Replacement: NBK twice played a key role in the replacement of Kuwait's local currency. The first was in May 1959, when the Indian rupee was replaced by what became known as the Gulf rupee. And again in 1961, when the Monetary Council withdrew the Gulf rupee and introduced the Kuwaiti dinar as the unit of exchange of the newly independent sovereign state of Kuwait and asserted control over its fiscal affairs.

The Invasion: The Iraqi invasion in 1990 was one of the greatest challenges in Kuwait's history. Despite the unanticipated devastating incident, NBK's Board of Directors called for an urgent meeting in the bank's London branch and was able to transfer its operations abroad and meet all its commitments to clients and other international banks. This step further proved NBK's resilience in times of crisis and strengthened its reputation for reliability and trustworthiness both at home and abroad.

Contributing to the Kuwaiti Economy: The liberation in 1991 demanded different services from NBK

The opening ceremony of NBK's first head office in 1963.

First NBK team, 1953.

which, was well-trusted by the financial markets. In October 1990, the bank became the Central Bank representative in the inter-bank agreement for all Kuwaiti banks. NBK successfully developed a special mechanism to pay the interest on behalf of Kuwaiti banks as well as provide international transfers. The 1990s were a golden era for the bank, during which NBK was able to extend and manage huge loans including one of $5.5bn to the government of Kuwait, the largest ever loan at the time in the Arab world.

Global Financial Crisis: NBK proved its resilience and fundamental strengths not only in the Souq Al-Manakh crisis and after the Iraqi invasion but also in the recent global financial crisis and the period of regional political instability. NBK not only survived but thrived. It has continued to operate profitably, exceeding all expectations thanks to the conservative policy of the bank with regard to risk management, to a clear strategic vision as well as its experienced and stable management.

Strong Financial Position and Excellent Results...

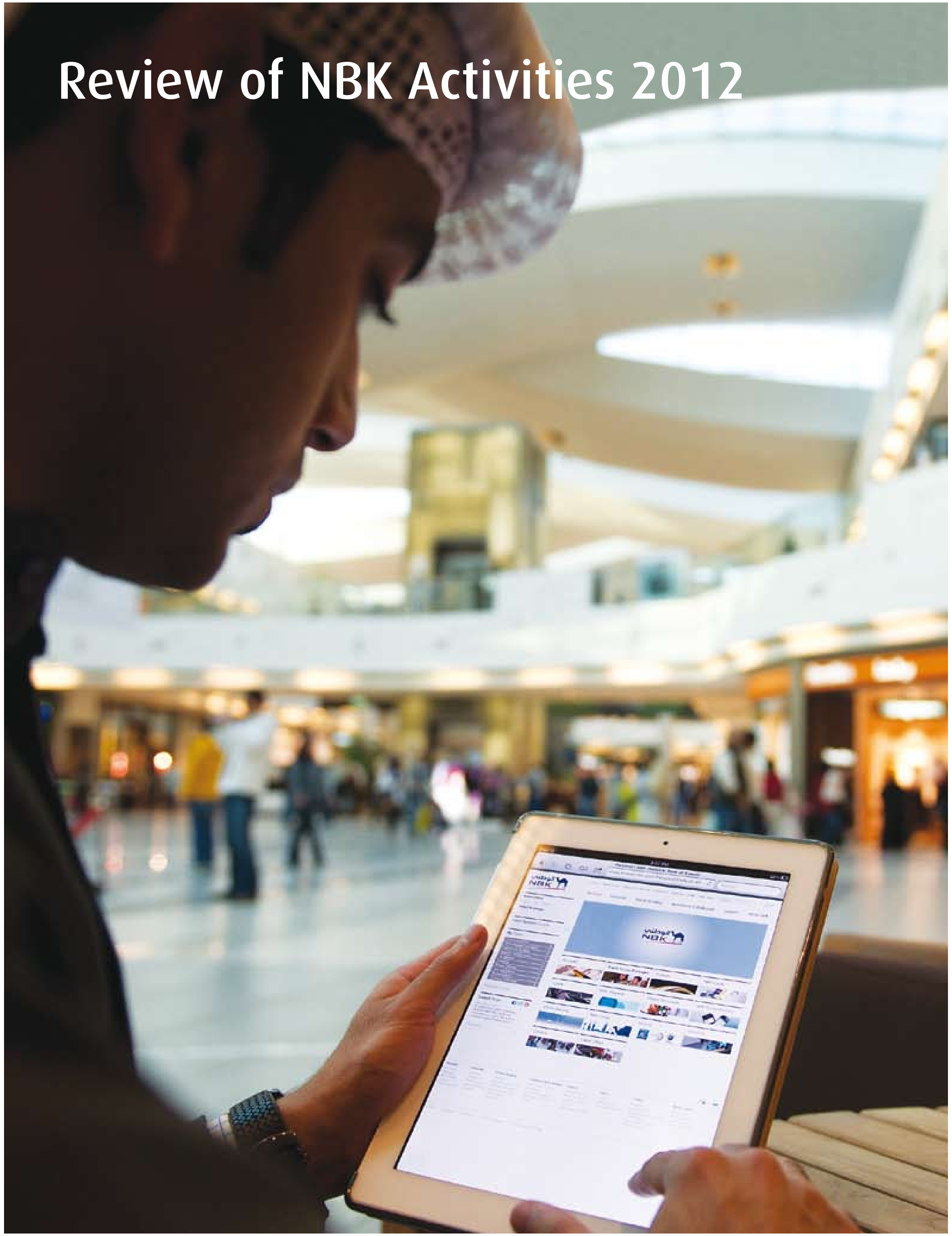
Each challenge posed different problems but NBK faced them all by remaining true to its conservative strategy at all times. It is still strengthening the bank's position in the market. As a result, NBK has continued to hold the highest ratings of any bank in the Middle East. This is reflected in financial results and consequently value creation to shareholders. NBK was established with a capital of 980 thousand Kuwaiti Dinars growing to a shareholders' equity of 2.3 billion Kuwaiti dinars in 2012.

Regional Expansions...

NBK's policy of expansion is the cornerstone of its strategic vision for diversifying its sources of income. Its regional and international presence is one of the largest among Arab banks. The bank now has 64 branches in Kuwait as well as branches, representative offices and subsidiaries in New York, London, Paris, Geneva, Singapore, Turkey and China as well as Egypt, Lebanon, Bahrain, Jordan, Qatar, the UAE, Iraq and Saudi Arabia.

NBK has undertaken a glorious journey over the past 60 years, proof of its resilience and financial strength which have underpinned its record of excellence. It is a journey not only for this bank to be proud of, but also for Kuwait and the Gulf region.

Review of NBK Activities 2012



Consumer Banking Group

In 2012 we have maintained our position of leadership in Kuwait. With a 40% share of the domestic market, NBK continues to be recognized as the leader in retail banking.

Our leadership stems from our focused pursuit of a two-pronged, customer-led strategy. This strives to meet the needs of strategic segments of the consumer market while differentiating our offering with value-added products and services which build customer satisfaction and loyalty. This approach has enabled NBK to establish a leading market share of most of the segments it serves, including markets for young people—reflecting their preponderance in the demographic makeup of the economy—fresh graduates, professional people, the affluent and high income customers.

Thanks to its targeted marketing campaigns, NBK enjoys the highest brand recognition in the financial services sector and is one of the leading brands in all industries in Kuwait. Our name is typically identified with strength, confidence and trust. It is associated with leading the industry in service quality, convenience and the rich array of products offered coupled with innovative technology. We are growing our business in a more balanced way, with a greater focus on organic growth.

We stand united as one business under a common theme “I am NBK”. This states that our customers’ success is our success. We are focused on providing our customers with the best service anytime and anywhere they do business with us. Our commitment to “enabling our customers to touch us” at their convenience is demonstrated in our channel management strategy.

We have now over 100,000 customers using online services and we continue to invest in making online services a better experience for our customers.

In 2012, our businesses, including Loans, and Deposits, generated record results and gained strong momentum.

Our credit cards have profited from the high use and spending on Thahabi and other products. We are experiencing high cards spending, including credit, prepaid and debit due to increasing customers’ reliability on our cards offerings. We have also continued to strengthen the Thahabi brand by providing comprehensive investment and banking options. Our exclusive Master Card World premium card for Thahabi customers has continued its success.
We are continually reengineering processes as an ongoing process embedded in our operating culture. Key to deepening our client relationships will be the benefits of emerging technology. As we respond quicker, communicate more effectively, simplify transactions, and innovate faster, we will be able to provide superior service to our customers. The more we harness emerging technologies, the easier it will be for our clients to work with us. As our customers increasingly incorporate technology into their financial routines, CBG will be positioned to capitalize on this by building technological innovation.

We are actively enhancing digital banking options (i.e., mobile banking systems, WOL and SMS) at an exceptional pace to meet or exceed those demands and continue our evolution as the best provider of digital banking.

The difference between success and failure in our business is the quality of the people who work with our customers. Consumer Banking Group (CBG) has the single largest pool of talent in our businesses. We manage our talent effectively by rewarding the high performers and by putting the right people in the right positions. Our goal is to empower our business leaders and create a more demanding performance management system to instill a meritocracy at every level.

Private Banking Group

Private Banking has remained the preferred wealth management provider for generations of Kuwaiti families. Professional expertise, integrity, confidentiality and trustworthiness are the cornerstones of our relationship with our clients.

The Group has strengthened its leading position in this market segment through a wide portfolio of innovative private banking products and services tailored for its client base. Private banking saw a steady increase in its Assets Under Management (AUMs) in 2012 despite the regional political turmoil and weakening economies in the international markets. Adhering to the bank’s conservative strategy, Private Banking continued to advise clients to maintain safe and secure investments and built on these strong and trusted relationships.

The Private Banking Group continued to leverage NBK’s international network extending its services to clients in Beirut, Cairo, Dubai, Geneva, London, Manama, New York and Paris. NBK continued to implement industry best practices in asset allocation and risk profiling. The Bank’s product line includes enhanced regional and international brokerage capabilities and regional (MENA) discretionary portfolio management mandates.

In 2012, Private Banking expanded advisory fixed income capabilities, assisted clients in locating and investing in prime properties in the United Kingdom and the United States and actively promoted Trust and other offshore services.

Corporate Banking Group.

NBK Corporate was able to make the most of the strengths of the group—long standing presence, in-depth knowledge of the market, strong relationships with public and private sectors, underpinned by an unrivalled reputation for reliability and sound risk management—to provide comprehensive cross-border banking solutions for the region's top corporations. Whether in financing, international trade, cash management or advisory services, we delivered.

Since 1991, the market share of foreign companies doing business in Kuwait on average has been in excess of 70%. In 2012, we maintained that dominant position. We also maintained a leading market share in trade finance of around 40%. The continuing turmoil in world markets only went to reinforce our strengths as one of the safest banks in the world. This hard won reputation helped us keep our name as the most sought after bank for regional corporations.

We outperformed our competitors in client relationship management, service delivery, corporate transaction banking platform (Watani Online Corporate or WOLC), Trade finance products and services, and many other areas. The results of 2012 Corporate Customer Satisfaction survey substantiate our leading market position. We out-performed our competition in almost all areas. Additionally, when compared to previous years' results, overall satisfaction experienced by NBK corporate customers rose by a significant amount.

The political and economic climate in 2012 was challenging. Government spending on infrastructure and non-oil projects under the five-year development plan was severely disrupted. Notwithstanding the difficult operating environment, we still achieved some good results. We have capitalized on our strategic client relationships to be their partner of choice for their expansion plans and have increased our market share with them. We have also attracted new clients in the medium sector and were pretty successful at that with a hit rate of 14%. We have also maintained our lead position in the regional market by advising Qtel on the Wataniya Telecom acquisition as well as arranging financing and foreign exchange transactions for the deal.

Our Trade Finance and WOLC units have upgraded their offerings too. In Trade Finance, we made the most of our unrivalled expertise in complex documentary credit transactions. Our products have commanding market share due to sophisticated service quality and complete product offering support, significant in depth market knowledge and international presence. WOLC offers the most complete regional cash management system and added functionalities to meet client requirements by upgrading to new technology, security, and performance standards. Financial transactions by corporate clients grew by 16%.

Our ongoing strategic development of capabilities shall continue in 2013. Our clients have enjoyed our customer centric approach and in return we have enjoyed their loyalty and business. We are most responsive to our clients' need and are ready to be at the forefront of any lending activity once it picks up, including government projects under the five year development plan and other private landmark projects.

Treasury

Liquidity management remains a top priority for Group Treasury especially in light of the prevailing global market conditions and fears of further deterioration in the debt crisis in the Euro Zone. Group Treasury has been actively working on improving the bank's funding profile, diversifying its funding sources as well as improving the health of its liabilities.

NBK's funding costs remained the lowest relative to the regional and international counterparts. On the other hand, the local market remained awash with excess liquidity, both in local and foreign currencies. Client activity in foreign exchange remained subdued on the back of stagnant economic growth and the absence of sizable government capital spending. That being said, NBK continued to be the bank of choice for mega foreign exchange deals. Our fixed income portfolio saw notable increases in 2012, despite our rigid investment criteria.

Treasury continued to offer advanced training courses, including leading-edge online courses.

KONDOR+, Treasury's From Office system, was successfully upgraded to the newest state-of-the-art version.

NBK Capital

In 2012, NBK Capital maintained its position as leading local and regional investment bank. It has four lines of business: investment banking, alternative investments, asset management and brokerage & research.

Investment Banking

In 2012, NBK Capital's Investment Banking Group reasserted its status as preferred advisor on mergers & acquisitions, listings, equity raising, debt and restructuring.

Investment Banking Group advised Qatar Telecom (Qtel) on the KD 519 million acquisition of 39.61% of National Mobile Telecommunications Company (Wataniya Telecom Kuwait). The transaction received CMA approval and was completed successfully in October. This was the largest acquisition in the GCC in 2012 which reaffirmed the Group's position at the top of the league tables.

NBK Capital's investment banking team also advised Kout Food Group, a leading food and beverage company, on a cross border acquisition in the United Kingdom. The transaction completed successfully in May 2012.

The Group also advised on the restructurings of approximately $ 1 billion of borrowings, including equity injections, bank debt, bonds and sukuk for two Kuwaiti companies and was joint bookrunner and joint lead manager for the KD 80 million bond issued by Kuwait Projects Company (KIPCO). This was the largest corporate bond ever in the local market in Kuwait.

In December the Group announced the successful completion of a landmark KD100 million (c. USD 356 million) Lower Tier II Subordinated Bond Issued by Burgan Bank. This was the first bond of its kind in Kuwait and the largest bond ever raised by a private sector issuer with a tenor of 10 years, callable after 5 years. The bonds were issued at par with coupons paid semiannually in arrears, also the bond was rated BBB+ by Capital Intelligence. The ten-year subordinated LT2 bond was issued in a fixed rate of (5.65%) and floating rate (CBK DR+390bps capped at 6.65%) tranches. Along with a 25 basis point step up if not called. This tenor is the longest in Kuwait's history.

The Group continued with its advisory role for Viva Telecom Kuwait, a subsidiary of Saudi Telecom (STC), on its listing on the Kuwait Stock Exchange. The Group also continued advising, together with two international advisors, on Zain Iraq's IPO, which is expected to be the largest in Iraq's history. Investment Banking continued working with one of the leading family-owned FMCG businesses in Kuwait advising on an initial public offering.

Alternative Investments

The Alternative Investments Group continued to successfully deploy capital in private equity and mezzanine transactions during 2012. The funds under management continued to perform well and achieved strong returns for investors. The group is currently raising funds for its next private equity fund.

The Group deployed the remaining capital of NBK Capital Equity Partners Fund I, the firm's first private equity fund, into two transactions; (1) Bavet – a niche animal pharmaceutical distributer in Turkey and (2) Sanabel Al Salaam – a leading Arabic sweets and confectionery retailer and producer in Saudi Arabia. We successfully exited a private equity investment in Hanco, a leading car rental and fleet leasing business in Saudi Arabia.

The remaining portfolio companies in NBK Capital Equity Partners Fund I continue to perform well with valuations increasing year-over-year.

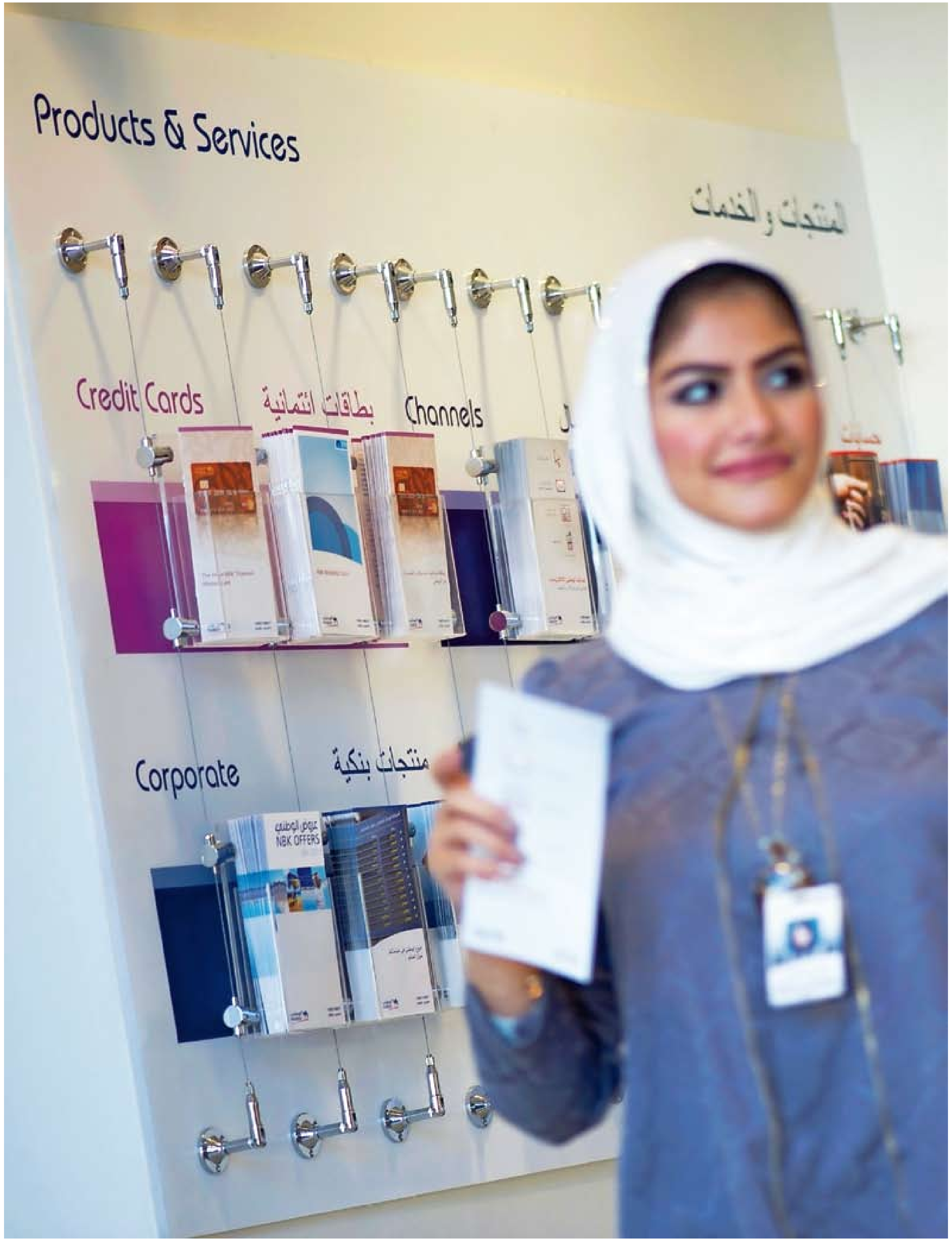
The team deployed more capital of NBK Capital Mezzanine Fund I, the firm's mezzanine fund, into Eikon International Holding, a leading university operator in Dubai. The remaining portfolio companies in NBK Capital Mezzanine Fund I continue to perform well and adhere to their respective covenant levels and payments.

Asset Management

Product Development: In 2012, the team was mainly focused on preserving capital and providing conservative, income producing funds to our clients during these turbulent global markets. We increased the frequency of reporting and regular updates to our clients as the year was occupied with macro events in the US and Europe. NBK Group's assets under management stood at $ 9.5 billion at year-end 2012.

MENA Equities: During the year the MENA Equities' team managed to increase the number of discretionary portfolios by 55%. The team has taken on several portfolios containing listed securities and restructured them into regional discretionary portfolios. The team also managed to attract several new High Net Worth and Institutional clients while increasing the product offerings by introducing a Dividend-Focused Separately Managed Account. In 2012, NBK Capital received the "2012 Qatar Equity Fund of the Year" award from the MENA Fund Manager Magazine.

Investment Advisory: The Investment Advisory team at NBK Capital provided regular updates to its clients on their investment portfolios through client meetings and comprehensive performance reporting, incorporating NBK's views on global economic and financial developments. Investment Advisory offered conservative, tailor-made fixed income portfolios in response to clients' demand for low risk, income-generating investments to mitigate against persistent market volatility. In addition to private client portfolio management services, Investment Advisory continued to build and enhance relationships with NBK Private Banking by serving as a conduit between private bankers and NBK Capital's lines of business. In doing so,



Investment Advisory provided value-added services to clients by generating referrals to our business partners to deliver a more compelling client experience while expanding the product mix of clients' portfolios, and enhancing the company's revenue streams.

Brokerage & Research

Research: During 2012, NBK Capital MENA Equity Research team increased coverage in existing sectors and added Egypt Banking and Real Estate sectors, as well as the MENA Petrochemicals and Fertilizers sector. Our research coverage was timely, with many of our updates featured in the press and on TV.

Brokerage: NBK Capital brokerage received "Best Broker of the Year in Kuwait for 2012" by Global Investor magazine in recognition of the leading market positions of Brokerage's three platforms (Online, HNW and Watani Financial Brokerage). The three platforms successfully navigated the transfer to the KSE's new trading system NASDAQ/OMX in May and the group unified its trading systems across the three units. In a complement to our leadership in regional trading, brokerage online platform added trading in Egypt's EGX in the fourth quarter of 2012 to its current six markets to offer its clients a "One account - Seven markets" service. NBK Capital Securities-Egypt, a joint-venture with Al Watany Bank of Egypt (AWB), extended the same brokerage offerings of NBK Capital to AWB's clients in Egypt. Moreover, NBK Capital Securities-Egypt will introduced Online trading services to AWB retail clients in Q4 2013.

International Banking Group

NBK's International Banking Group made an even greater contribution this year to the Bank's results, demonstrating once again the benefits of geographical expansion and diversification. NBK started its expansion outside Kuwait in the 1980s by opening full service branches in the region (Bahrain and Lebanon) and in the key international centers of New York, London, Paris, Geneva and Singapore. In 2004, NBK took the strategic decision to expand its presence in the Middle East and North Africa (MENA) region. The Bank has established branches in Jordan, Saudi Arabia (Jeddah) and the UAE (Dubai and now Abu Dhabi) and through acquisition entered simultaneously Qatar, Iraq, Egypt and Turkey.

Today, NBK has an ever expanding international network of subsidiaries and associates with 109 branches outside Kuwait. This network is complemented by a mix of alternative and remote distribution channels. All of the Bank's businesses outside Kuwait are successfully integrated. Most of these branches operate under the same brand and use the same IT systems.

NBK's network outside Kuwait provides clients access to a wide range of markets and investment offerings. The international mortgage program launched in 2011 is one example where financing is offered to high income households wanting to purchase a property in their country of choice (USA, France, UK, Dubai, Abu Dhabi, Lebanon, Jordan and Egypt). The Bank established its first center dedicated to servicing this sector at its Ras Salmiya branch, with the infrastructure needed to handle all customer transactions.

In 2012, NBK focused its efforts on GCC countries given the robustness of GCC economies relative to the turmoil elsewhere in the region and to the global financial crisis.

The Bank is increasing its presence in GCC member states. NBK currently operates in Jeddah, Dubai and Bahrain where it offers corporate clients and High Net Worth Individuals a range of treasury and wholesale banking credit solutions, both conventional and Sharia-compliant, in addition to trade finance services, and basic retail services including personal loans and NBK's Premier Thahabi. In 2012, NBK extended online banking services for its retail customers in Dubai and Bahrain. NBK also plans to open a new branch on Airport Road in Abu Dhabi in 1Q 2013.

In Qatar, the Bank operates through its associate International Bank of Qatar (IBQ). NBK has a 30% stake in IBQ and has led the bank's transformation from a single branch to a full service commercial bank through a management agreement signed in 2004. Currently, IBQ operates 10 branches and service centers in addition to 35 ATMs strategically located throughout Qatar. The bank has active corporate, retail and treasury departments in addition to a direct sales team. It has received several accolades that are testimony to its robust performance, notably Euromoney's "Best Private Banking Services" award 2012. IBQ customer service is supported by a fully-equipped platform including a 24/7 Call Center and online banking.

Outside the GCC, despite the challenging environment, NBK's customer base continued to grow, drawn by the Bank's strong brand values of quality, confidence and security.

In Egypt, NBK operates through Al Watany Bank of Egypt (AWB), the subsidiary acquired in 2007. Under NBK management, AWB is undergoing a full transformation to become one of the top foreign banks in the country.

In the last few years, the Bank has expanded and upgraded its branch network to 42 today, including 3 that are fully Sharia-compliant, and has doubled its

ATMs to 106. It has improved customer service and availability by establishing a call center and online banking services. Incoming calls and e-mails are now answered around the clock.

AWB's emphasis in 2012 was on stabilizing its operations amid the unrest while implementing its transformation program. In a very difficult year for the economy, loan losses remained at low levels. While business activity dipped overall, AWB's commercial network was busy taking new deposits and capturing new customers seeking the safety guaranteed by the bank's affiliation with NBK.

In Iraq, Jordan and Lebanon, NBK's focus was on enhancing IT and Network Infrastructure to continue to provide customers data protection and a reliable and secure platform for their accounts and transactions. There was continued emphasis as well during the year on staff security, especially in Iraq where there were spikes of violence. NBK operates in Iraq through its subsidiary Credit Bank of Iraq (CBI), in which the Bank owns a controlling 81% stake. CBI offers transfers and trade finance to Kuwaiti corporate clients and foreign contractors as well as basic retail products for Iraqi customers. It operates 14 branches throughout the country and is among the largest private banks in Iraq. In Lebanon and Jordan, the bank operates a small network of branches under the NBK brand strategically located to service niche customers for the bank.

In London, Paris, Geneva, New York and Singapore, NBK continued to see a strong inflow of deposits from HNWIs, financial institutions, oil companies, correspondent banks and government agencies, all seeking the safety they know they can obtain from NBK.

Risk Management and Governance

NBK has consistently maintained a strict, low-risk strategy towards the types of activities in which it engages and the types of exposures it takes on. This strategy of focusing on high–quality customers and banking products and services has served the bank well historically and continues to protect the bank even in times of unprecedented crisis in the global financial system. In 2012 the bank took numerous steps to improve its risk management function. These included the implementation of economic capital models to measure the bank's risk, in addition to using revised stress-testing and capital planning, and the development of a number of policies to deal with the group's overall risk management.

NBK plans to gain greater value from its competent risk management strategy. In particular, the bank is seeking further improvements in the development and refinement of rating models; more collection and analysis of historical loss data; the implementation of an Asset/Liability management system to improve interest rate and liquidity risk management. . In addition to the use of economic capital for capital adequacy assessment purposes, the bank is also exploring other potential uses for the risk measures such as performance measurement and risk-based pricing.

NBK highly values the role of corporate governance in improving the overall performance especially in the current environment. Corporate governance in NBK is a combination of internal and external practices aimed at reducing risk exposures while protecting and maximizing shareholders' value.

NBK's international advisory board, an unprecedented regional initiative, comprises a number of the world's most prominent leaders in the fields of politics, economics, and business. The board's main role is to provide the bank with the expertise and consultation needed in assessing the bank's future strategy. The board's role also expands to enforcing the founding principles of governance in NBK.

Human Resources

Human Resources is committed to recruiting Kuwaiti nationals as well as developing and strengthening the professional skills of all employees and 2012 was yet another successful year for HR.

For the third year in a row, the NBK High Fliers Program trained 25 staff in leadership skills. The NBK Special Bridge Program developed participants in technical knowledge in accounting and banking & finance to prepare them for the High Fliers-Cohort IV program. HR provided continuous learning through refresher courses to Cohort I, II and III alumni to keep them up to date on the latest in management learning and leadership development.

Mentoring workshops were organized by Human Resources to transfer knowledge and insight from experienced leaders to future leaders on how to apply their skills in new and better ways as well as how to take calculated risks. A development program for middle managers was devised to hone their people management skills, to share their experiences and challenges with each other, to effect change in ways of managing, to propose solutions and to identify potential communication champions.

Human Resources Group sent 65 fresh graduates to the NBK Academy for their induction in the fundamentals of consumer lending, financial accounting, ethical issues, marketing, assertiveness and other skills. NBK also introduced the Shabab program to develop young Kuwaiti holders of diplomas for their initial training in banking. There were fifteen participants in this program in 2012 with a plan to more than double that figure next year. The Institute of Banking Studies (IBS) ran certification programs for 140 NBK employees to develop their technical skills and improve their English.

In addition, specialist training was provided to enhance staff creativity. Human Resources provided group-wide training and professional development for a range of soft skills, financial analysis, product understanding and computer skills.

Complying with the government's Kuwaitization requirements of 60%, NBK recruited across the group more than 300 Kuwaitis for senior and junior posts. Furthermore, NBK was recognized with an award for the employment of nationals. Kuwait is the second most successful state in the Gulf Cooperation Council (GCC) at achieving localization targets.

Our Human Resources initiatives were extended to our international operations. Several trainings were initiated in most of our regional operations to raise technical levels and the standards of working practices.

A key initiative was a successful Credit Training Program for 18 participants from Kuwait and MENA locations to improve their Corporate/Credit technical skills and to standardize and enhance Credit proposal and analysis. The training also provided an excellent networking opportunity so that people could meet colleagues doing similar work in different locations. Another course on credit was specially designed and delivered for 13 AWB Credit Officers.

NBK and the Community

The year 2012 marked National Bank of Kuwait's 60th anniversary. NBK celebrated the occasion under the slogan 'serving Kuwait for 60 years' a testimony of our contribution to the economic growth and development of Kuwait. In 2012, NBK reinforced its position as a lead contributor to the development of the Kuwaiti society through its commitment to corporate social responsibility. This commitment became evident in the numerous cultural, community and social activities and charities the bank supported throughout the year.

NBK gives top priority to healthcare in Kuwait. Over the years, NBK has engaged in numerous activities and initiatives to support the healthcare sector in Kuwait based on the belief in its mission towards the society. NBK children's Hospital represents the most remarkable initiative launched by NBK. The hospital provides medical care for children suffering from chronic diseases.

In 2012, NBK donated KD 4 million for the hospital's expansion and the establishment of a specialized pediatric leukemia treatment center. NBK also supports the transfer of knowledge and skills by hosting teams of experts from abroad. In 2012, NBK funded a visit by a British medical team from the prestigious Great Ormond Street Hospital in London, which included several specialists in blood disease, cancer and Pediatric Neurosurgery to work at the NBK Children's Hospital.

Also in 2012, NBK continued to promote health care and awareness for its staff and customers through various programs including its Breast Cancer Awareness and Prevention Campaign, 'Be Aware...Get Checked Today' aimed at its female staff and clients.

For more than 20 years now, NBK has implemented charitable, social and philanthropic programs during the Holy Month of Ramadan. In 2012, we sustained our most prominent and successful Ramadan program 'Do Good Deeds in Ramadan' which comprised of a series of activities and events aimed at motivating community engagement and charity in Kuwait.

In the field of education, NBK continued its support for Kuwait's youth honoring outstanding high school graduates of Kuwaiti schools for the school year 2011-2012. Also during the year, NBK sponsored the 29th Annual Congress of the National Union of Kuwaiti Students (NUKS) in the United States and hosted several groups of visiting school and university students in Kuwait on field visits.

Environmentally, NBK deems protection and conservation of the environment an important aspect of corporate social responsibility. NBK's 'Think Twice' environmental campaign, now in its sixth year, encourages the Kuwait community to adopt sustainable practices for protecting the environment and conserving energy through a range of initiatives including beach and desert clean up campaigns, electricity conservation programs and other efforts.

Economic and Financial Developments in the MENA and Kuwait in 2012

MENA and the GCC:

2012 was a year of varying economic conditions across the MENA. Some economies did well, some disappointed and others were negatively affected by social disorder and military conflict.

While activity in Libya recovered relatively swiftly from the revolution of 2011, war in Syria has devastated the local economy and risked spilling over to neighboring countries. The Egyptian economy managed to see some sort of stability, though concerns over capital flight and the direction of economic policy persist. In the resource-rich GCC, meanwhile, economic growth is expected to have remained solid, supported by strong oil receipts and – in some cases – high levels of government investment. Even here, however, the challenges of delivering on vast capital expenditure commitments have been visible. Growth in the GCC is expected to have reached 5.4% in 2012, compared to 5.3% for MENA as a whole.

High oil prices continued to provide a positive economic backdrop for the GCC region. Brent crude averaged $112 pb in 2012, close to the record $111 average of 2011. Given the fragile world economic picture, growth in global oil demand was modest. However, disappointing non-OPEC supply, geopolitical tensions in the Middle East and loose monetary policy in the advanced economies all combined to keep oil prices high. Oil production was also strong across the GCC. OPEC maintained high production levels to cap upward pressure on oil prices, which it saw as a threat to the world economy. This meant that oil output in both Saudi Arabia (10 mbpd) and Kuwait (3 mbpd) reached levels not seen for decades. Overall hydrocarbon output in the GCC grew by 5.2%, while strong oil receipts helped to support already impressive fiscal and trade balances.

Outside the oil sector, economic conditions were mixed, with growth fastest in countries hit least by the financial crisis and where government investment has been strongest – namely Saudi Arabia, Qatar and Oman (real non-oil growth of 5-9%). In other GCC states, the impact of corporate and personal sector deleveraging has been larger, and government policy has been more subdued or constrained. In the UAE, for example, the weak real estate sector and ongoing corporate debt restructuring continue to depress lending growth and business investment, while financially-strapped Dubai and Federal governments carry on tightening their belts. In Bahrain, the economy has seen a return to moderate growth following the disturbances of 2011. But a lack of oil resources has seen fiscal pressures intensify, while global events and competition from neighboring countries present challenges for its international banking sector.

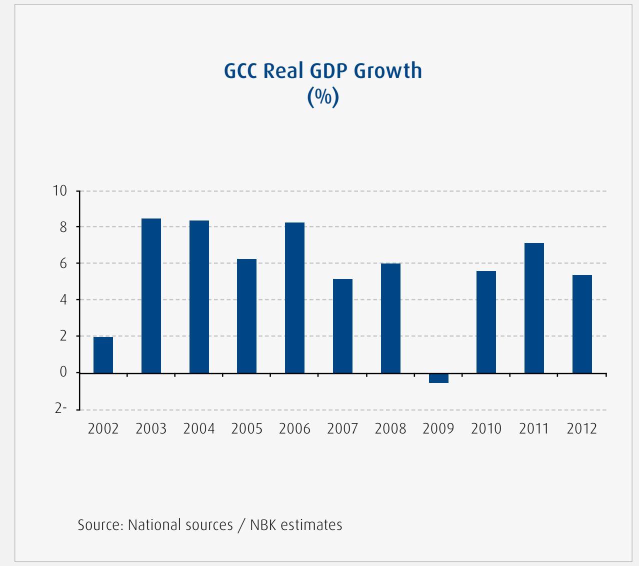
The region continues to look somewhat shielded from further turbulence in the global economy, including Europe. Banks are well capitalized and have little direct exposure to any possible European sovereign default. Economic growth is more measured than before, the aggregate fiscal position is very strong, and most governments are committed to medium-term development plans that will support domestic demand. In the GCC, the UAE looks most exposed, particularly in Dubai. Given its strong trade and financial links, it is more vulnerable to changes in the global economy, while its indebted corporates could face refinancing difficulties if funding conditions tighten. It is also an important trading partner for Iran, whose economy is weakening under international sanctions. Recent trade data, however, suggest that it is weathering these challenges reasonably well.

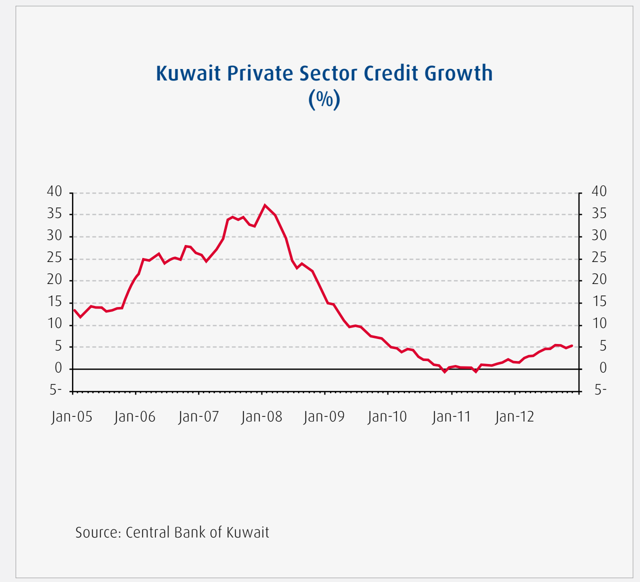
Regional markets fared better in 2012 than in the previous year. Social and political instability across the region weighed on financial markets' performance in 2011 but regional markets rebounded in 2012 and the S&P Pan Arab Composite was up 4%. Still, the performance of financial markets varied widely across the region. The Egyptian stock market fared the best with the S&P Egypt index up 41% from its close in 2011. Egyptian equities saw a relative recovery as parliamentary elections went ahead reasonably smoothly. The UAE was the second best performing market regionally, up a good 24%. Meanwhile, the S&P Jordan was off 5% on the year. Oman and Bahrain S&P indices both dropped 4%.

Kuwait:

Economic growth was maintained at a decent pace in 2012 thanks largely to the oil sector, where prices and production remained close to historic highs. Real GDP growth was estimated at 6% in 2012, with growth in the oil sector reaching 10%. Outside the oil sector, growth was a more modest 4%. Slow implementation of government infrastructure projects, continued corporate sector deleveraging, an unsettled political environment and lack of progress on economic reforms continued to weigh on the business climate. The uncertain global economic environment also affected business confidence.

There were some bright spots in the domestic economy. The consumer sector enjoyed a further





year of strong growth, fuelled by high employment levels and earlier pay and benefits increases for nationals – though growth in the latter may now be easing. The value of point-of-sale transactions rose 14% y/y in 3Q 2012, following spectacular growth of 31% in 2011. The real estate sector also continued to do well. The value of residential transactions in 2012 rose 12% y/y, with much of this driven by land sales. Activity in the apartment sector was stronger still, as investors continued to look for yield in light of an underperforming stock market.

These broad economic patterns were reflected in monetary conditions. Overall credit growth saw slight signs of improvement, but remained weak overall, averaging 4% y/y in 2012. Within this total, credit to the consumer sector (excluding securities purchases) rose by an impressive 14%. By contrast, credit to the rest of the economy grew by just 1%, depressed by continued deleveraging by investment companies and a lack of progress in implementing the government's 4-year development plan. Private deposit growth stood at a soft 6% over the same period helped by large increases in short-term deposits. But this average masked an acceleration as the year went on.

In October, the Central Bank of Kuwait cut its main lending rate by 50 bps to 2.0% in an attempt to stimulate loan growth – the first cut since early 2010. Deposit rates were left unchanged. The lending rate has now fallen 4.25 percentage points from its peak of 6.25% in January 2008. Given the structure of the Kuwaiti economy and the lack of good current lending opportunities, however, the latest rate cut by itself was not expected to have a large impact on credit growth. Moreover, the scope for monetary policy activism remained constrained by the need to manage the exchange rate system, in which the dinar is pegged to a basket of currencies including the US dollar.

Fiscal policy has been broadly supportive of the economy, with strong oil revenues and vast reserves providing the government with ample resources to finance increases in spending. Government spending (excluding transfers to the social security fund) fell by 1% in FY 2011/12, following the giant

38% increase seen the previous year, which was boosted by the KD 1,000 per national Amiri grant. This fall incorporated a 20% increase in spending on (non-military) wages and salaries, which rose 20% y/y. Capital spending, by contrast, fell 2% and came in at just 64% of its budgeted allocation – the second weakest performance of the past ten years.

The budget for FY 2012/13 was heavily delayed by the uncertain political environment and as a result, saw a lower total spending target than might have been approved at the beginning of the year. Spending was set to rise 9% in budget-on-budget terms. While the overall fiscal stance therefore remains supportive, the first 9 months of the year saw few signs of a significant pick-up in spending on much-needed infrastructure projects.

Similarly, spending under the government's 4-year, KD 31 billion development plan (FY2010/11 to FY2013/14) has continued to disappoint, affected by a combination of technical, administrative and political hurdles. Public spending in the second year of the plan (FY2011/12) was expected to have come in at around 60% of the KD 5.2 billion originally targeted – similar to the 62% spending rate seen in year 1. Targeted public spending for year-3 was set at KD 5.5 billion, an increase of 5%. The first of the plan's ambitious public-private partnership (PPP) projects – the North Zour Independent Water and Power Project – was awarded in 2012 and a joint venture company has been formed. Most other PPPs remain at a much earlier stage of the project cycle.

Inflation averaged 2.9% y/y in of 2012, down from 4.8% in 2011. The decline was driven by decelerating food price inflation, resulting from a fall in global food prices. However, core inflation (which excludes food) was also very low, at 2.2%. Inflation is being kept low by a combination of sluggish economic performance, modest monetary growth, the lagged effect of a stronger US dollar on import prices and greater cost consciousness across the corporate sector than during the boom years. These factors more than compensate for consumer sector strength. A modest rise in inflation is expected for 2013, but not enough to generate concern amongst policymakers.

For Kuwaiti banks, 2012 was another challenging year. Relatively weak business activity and some unresolved asset quality issues continued to reduce profitability. Total bank profits for the nine months ending September 2012 were down 5% year-on-year (June 2012: down 12%). Higher provisions were the main reason for the drop in profits, as banks were encouraged to take more precautionary reserves for unforeseen loan losses. The absence of growth in business lending has also hurt bank earnings with delays in government projects the main culprit.

Capital Markets Authority:

The Capital Market Authority (CMA) became more organized and more fully staffed in 2012 as the oversight and regulatory authority of the Kuwait Stock Exchange transfer was complete. The newly established authority oversaw and finalized several pending legislative and compliance measures. The CMA was established in 2011. Kuwait's parliament had passed new legislation for the formation of an independent authority to supervise and regulate the country's securities exchange and financial markets in 2010. The CMA was long awaited, and may still be going through some teething problems. However, investors do expect that, gradually, the CMA's benefits will flow to better run markets, and will further support investor confidence. In particular, foreign investors and others that had shied away in the past, for legal or trust-related reasons, may decide to revisit the KSE, more so if this also coincides with an improved economic policy outlook.

Risk Management

Risk Management

In December 2005 the Central Bank of Kuwait (CBK) issued directives on the early adoption of the Capital Adequacy Standards under the Basel II framework applicable to licensed banks in Kuwait. These directives set out the capital adequacy rules for calculating and maintaining the minimum capital required for credit, operational and market risks under the "Standardised Approach". The CBK Basel II framework is intended to strengthen risk management and market discipline and to enhance the safety and soundness of the banking industry in Kuwait. Furthermore, in June 2009, CBK issued its circular amending & replacing the section covering "Capital Adequacy Assessment Process". The new amendments related mainly to Pillar two of Capital Adequacy Standard pertaining to the Supervisory Review Process and emphasised the importance of Internal Capital Adequacy Assessment Process (ICAAP) performed by banks. As such, and in compliance with the aforementioned instructions, National Bank of Kuwait S.A.K. (NBK) has developed an ICAAP and Stress Testing framework along with its underlying models, policies and procedures. NBK continually enhances its ICAAP and Stress Testing framework to maintain its capital commensurate with the overall risks to which the Bank is exposed.

1. GROUP STRUCTURE

The core activities of NBK and its subsidiaries (collectively the "Group") are retail, corporate and private banking, investment banking, and asset management & brokerage services. For further details on the Group's activities, please refer to note 3 of the Group's consolidated financial statements.

The consolidated financial statements and capital adequacy regulatory reports of the Group have been prepared and consolidated on a consistent basis, save as otherwise disclosed. For additional information on the basis of preparation and basis of consolidation please refer to notes 2.1 and 2.3 of the Group's consolidated financial statements.

A brief description of the Bank's principal subsidiaries is as follows:

- **NBK (International) plc (United Kingdom)** is a wholly owned subsidiary of the Bank with two offices in London and one in Paris which provides retail, private and corporate banking, treasury and trade finance related services.
- **NBK (Lebanon) S.A.L. (Lebanon)** is 85.5% (2011: 85.5%) owned by the Bank and provides retail, commercial and private banking and real estate related services through a network of eight branches.
- **NBK Banque Privee (Suisse) S.A. (Switzerland)** is a wholly owned subsidiary of the Bank headquartered in Geneva. In addition to traditional banking services it provides portfolio management services and family trust, advisory and custody services to individuals with high net worth and to institutions.
- **Credit Bank of Iraq S.A. (Iraq)** is 81.0% (2011: 80.1%) owned by the Bank and provides retail and commercial banking services through a network of fourteen branches in Iraq.
- **National Investors Group Holdings Limited (Cayman Islands)** is a wholly owned subsidiary of the Bank and was established as an investment company.
- **Watani Investment Company K.S.C (Closed) (Kuwait)** is 99.9% (2011: 99.9%) owned by the Bank and provides corporate finance, private equity and debt capital markets services.
- **Al Watany Bank of Egypt S.A.E** is 98.5% (2011: 98.5%) owned by the Bank and provides retail, private and corporate banking, treasury and trade finance related services through a network of forty two branches.
- **Watani Financial Brokerage Company (Closed)** is 86.7% (2011: 86.7%) owned by the Bank and provides brokerage services.
- **Boubyan Bank K.S.C (Kuwait)** is 58.4% (2011:47.3% associate) owned by the Bank and provides banking services in Kuwait through a network of twenty two branches, in accordance with Codes of Islamic Sharia'a. It is licensed by the CBK.

2. CAPITAL STRUCTURE

The Group's regulatory capital comprises (a) Tier 1 capital which is considered as the core measure of the Group's financial strength and includes share capital, reserves, retained earnings and non-controlling interests (net of treasury shares and goodwill) and (b) Tier 2 capital which consists of the allowed portions of revaluation reserves and general provisions.

The Bank's share capital as at 31 December 2012 comprised 4,353,497,625 issued and fully-paid up equity shares (2011: 3,957,725,114). The total regulatory capital for the Group was KD 1,717,593 thousand (2011: KD 1,570,414 thousand). Tier 1 and Tier 2 capital were KD 1,657,408 thousand and KD 60,185 respectively (2011: KD 1,570,414 thousand and KD nil respectively) as detailed below:

KD 000's

Tier 1 capital	31 December 2012		31 December 2011	
Share capital		435,349		395,772
Proposed bonus shares		21,768		39,577
Reserves:				
Statutory reserve	217,675		197,886	
Share premium account	699,840		699,840	
Treasury share reserve	17,957		20,403	
General reserve	117,058		117,058	
		1,052,530		1,035,187
Retained earnings		864,498		729,601
Foreign currency translation reserve		(35,522)		(33,032)
Share-based payment reserve		12,313		10,469
Non-controlling interests in the equity of subsidiaries		121,496		11,965
Deductions from Tier 1 capital:				
Treasury shares		(79,171)	(33,415)	
Significant minority investments (50%)		(67,700)	(110,146)	
Goodwill		(668,153)	(473,559)	
Shortfall transferred from Tier 2 capital			(2,005)	
				(619,125)
Total Tier 1 capital		**1,657,408**		1,570,414
Tier 2 capital				
Revaluation reserves		11,952	10,511	
General provisions		115,933	97,630	
Significant minority investments (50%)		(67,700)	(110,146)	
Shortfall transferred to Tier 1 capital			2,005	
Total Tier 2 capital		**60,185**		0
Total eligible capital base		**1,717,593**		1,570,414

3. CAPITAL ADEQUACY RATIOS

The Group's total capital adequacy ratio as at 31 December 2012 was 16.98% and Tier 1 ratio was 16.39% (2011: total capital adequacy ratio was 18.29% and Tier 1 ratio was 18.29%) against regulatory requirements of 12%. The Group ensures adherence to CBK's requirements by monitoring its capital adequacy against higher internal limits. This process is supported by the use of proprietary capital-planning methodology.

Risk Management Continued

3. CAPITAL ADEQUACY RATIOS (Continued)

Each banking subsidiary is directly regulated by its local banking supervisor which sets and monitors its capital adequacy requirements. In addition, CBK monitors capital adequacy at the Group level.

The Tier 1 and total capital ratio of the banking subsidiaries were as follows:

	31 December 2012		31 December 2011	
Subsidiary Banks	Tier 1 ratio	Total capital ratio	Tier 1 ratio	Total capital ratio
NBK (International) plc (United Kingdom)	25.19%	26.79%	30.78%	31.58%
NBK (Lebanon) S.A.L. (Lebanon)	29.26%	30.64%	25.68%	27.44%
NBK Banque Privee (Suisse) S.A. (Switzerland)	65.31%	67.46%	78.22%	79.74%
Credit Bank of Iraq S.A. (Iraq)	172.80%	174.50%	132.49%	133.95%
Al Watany Bank of Egypt S.A.E. (Egypt)	18.28%	19.17%	16.39%	17.13%
Boubyan Bank K.S.C.(Kuwait)	23.85%	24.39%	-	-

Other than restrictions over transfers to ensure minimum regulatory capital requirements are met there are no further impediments on the transfer of funds or regulatory capital within the Group.

4. PROFILE OF RISK-WEIGHTED ASSETS AND CAPITAL CHARGE

The Group's risk-weighted capital requirement for credit, market and operational risks are shown below. The calculations for 31 December 2012 include Boubyan Bank K.S.C., an Islamic Banking subsidiary acquired during the year (note 26 of the consolidated financial statement). For purposes of determining risk-weighted assets and capital required, exposures and assets at Boubyan Bank K.S.C. are risk-weighted, and capital charge calculated, in accordance with CBK regulations applicable to banks providing banking services compliant with Codes of Islamic Sharia'a. Those figures are then added to corresponding figures pertaining to all the rest of the Group, identical with the treatment in relevant reports submitted to the CBK.

4.1. Credit risk:

The total capital charge in respect of credit risk as at 31 December 2012 was KD 1,093,443 thousand (2011: KD 925,132 thousand) as detailed below:

KD 000's

	31 December 2012			31 December 2011		
	Gross credit exposure	Risk-weighted assets	Capital charge	Gross credit exposure	Risk-weighted assets	Capital charge
Cash	118,130	-	-	105,588	-	-
Claims on sovereigns	3,050,364	99,293	11,915	2,490,898	76,809	9,217
Claims on public sector entities	381,449	41,656	4,999	297,985	39,310	4,717
Claims on banks	2,847,315	687,897	82,548	2,262,399	534,528	64,143
Claims on corporates	8,299,385	4,878,391	585,407	7,155,864	4,370,791	524,495
Regulatory retail exposure	2,996,648	2,772,948	332,754	2,312,545	2,230,477	267,657
Past due exposures	150,533	53,076	6,369	72,561	60,267	7,232
Other exposures*	728,240	578,766	69,451	498,211	397,251	47,670
Total	18,572,064	9,112,027	1,093,443	15,196,051	7,709,433	925,132

* Other exposures above includes an amount of KD 162,638 thousand negative (2011: KD 100,960 thousand negative) representing the amount of general provision in excess of the 1.25% allowed as a contribution towards Tier 2 capital.

4.2. Market risk:

The total capital charge in respect of market risk was KD 30,979 thousand (2011: KD 30,666 thousand) as detailed below:

KD 000's

	31 December 2012 Capital charge	31 December 2011 Capital charge
Interest rate risk	3,130	2,977
Equity position risk	-	-
Foreign exchange risk	27,849	27,689
Total	30,979	30,666

4.3. Operational risk:

The total capital charge in respect of operational risk was KD 89,130 thousand (2011: KD 74,470 thousand) This capital charge was computed by categorising the Group's activities into 8 business lines (as defined by the Basel II framework) and multiplying the business line's three-year average gross income by a pre-defined beta factor.

5. RISK MANAGEMENT

The complexity in the Group's business operations and diversity of geographical locations require identification, measurement, aggregation and effective management of risks and efficient allocation of capital to derive an optimal risk and return ratio. The Group manages its risks in a structured, systematic and transparent manner through a global risk policy which embeds comprehensive risk management into the organisational structure and risk measurement and monitoring processes.

During 2009 the Group augmented its overall framework for governance and capital planning and management by undertaking an ICAAP, which includes "scenario testing" at periodic, regular intervals. In line with guidelines from the Basel Committee and CBK, key principles of the Group's ICAAP include:

- Responsibilities of the Board and Senior Management.
- Sound capital management
- Comprehensive assessment of risks.
- Monitoring and reporting.
- Control and review of the process.

The key features of the Group's comprehensive risk management policy are:
- The Board of Directors provides overall risk management direction and oversight.
- The Group's risk appetite is determined by the Executive Committee and approved by the Board of Directors.
- Risk management is embedded in the Group as an intrinsic process and is a core competency of all its employees.
- The Group manages its credit, market, operational and liquidity risks in a co-ordinated manner within the organisation.
- The Group's risk management function is independent of the business divisions.
- The Group's internal audit function reports to the Board Audit Committee and provides independent validation of the business units' compliance with risk policies and procedures and the adequacy and effectiveness of the risk management framework on a Group-wide basis.

The risk management function assists senior management in controlling and actively managing the Group's overall risk. The function also ensures that:
- The Group's overall business strategy is consistent with its risk appetite approved by the Board of Directors and allocated by the Executive Committee.
- Risk policies, procedures and methodologies are consistent with the Group's risk appetite.
- Appropriate risk management architecture and systems are developed and implemented.
- Risks and limits of the portfolio are monitored throughout the Group, including at appropriate "regional" levels.

The Group regularly assesses the adequacy and effectiveness of its risk management framework in light of the changing risk environment, including at its newly-acquired subsidiary (see note 26 of the consolidated financial statements).

5.1. Scope and nature of risk reporting tools

The comprehensive risk management framework enables the Group to identify, assess, limit and monitor risks using a comprehensive range of quantitative and qualitative tools. Some of these tools are common to a number of risk categories, while others are tailored to the particular features of specific risk categories and enable generation of information such as:

Risk Management Continued

5. RISK MANAGEMENT (Continued)

5.1. Scope and nature of risk reporting tools (Continued)

- Credit risk in commercial and consumer lending and other asset exposures, such as collateral coverage ratio, limit utilisation, past-due alerts, etc.
- Quantification of the susceptibility of the market value of single positions or portfolios to changes in market parameters (commonly referred to as sensitivity analysis).
- Quantification of exposure to losses due to extreme movements in market prices or rates.

The Group regularly assesses the adequacy and effectiveness of its reporting tools and metrics in light of the changing risk environment.

5.2. Risk management processes

Through the comprehensive risk management framework, transactions and outstanding risk exposures are quantified and compared against authorised limits, whereas non-quantifiable risks are monitored against policy guidelines and key risk and control indicators. Any discrepancies, excesses or deviations are escalated to management for appropriate action.

The key risks assumed by the Group in its daily operations are outlined below:

5.2.1. Credit risk

Credit risk is defined as the likelihood that a customer or counterparty is unable to meet the contracted financial obligations resulting in a default situation and/or financial loss. Credit risk arises in the Group's normal course of business.

5.2.2. Credit risk management strategy

The approach to credit risk management is based on the foundation to preserve the independence and integrity of the credit risk assessment, management and reporting processes combined with clear policies, limits and approval structures which guide the day-to-day initiation and management of the Group's credit risk exposure. This approach comprises credit limits which are established for all customers after a careful assessment of their creditworthiness.

Standing procedures, outlined in the Group's Credit Policy Manual, require that all credit proposals be subjected to detailed screening by the domestic or international credit management divisions pending submission to the appropriate credit committee. Whenever necessary, credit facilities are secured by acceptable forms of collateral to mitigate the related credit risks. The Board of Directors defines the Group's credit risk management strategy and approves significant credit risk policies to ensure alignment of the Group's exposure with its risk appetite.

5.2.3. Credit risk management structure

Senior management implements the Board of Directors' credit risk strategy and develops policies and procedures for identifying, assessing, monitoring and controlling credit risk.

The Group's Executive Committee, chaired by the Group CEO and comprising senior executives from the business divisions, meets regularly to review the Group's corporate and consumer credit portfolios and advises the Board appropriately.

5.2.4. Key features of corporate credit risk management

- Credit facilities are granted based on detailed credit risk assessments which consider the purpose of the facility and source of re-payment, prevailing and potential macro-economic factors, industry trends and the customer's positioning within its industry peer-group.
- In compliance with CBK regulations, lending to individual Board Members and related parties is fully secured and monitored by the Senior Credit Committee. Such transactions are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated parties. All such facilities are approved by the Board of Directors in line with the relative authorities from the Shareholders' General Assembly.
- Internal credit-rating models are regularly reviewed by the Group risk management function in co-ordination with line management and the Executive Committee and continually enhanced in line with industry credit risk management "best practices".
- All new proposals and / or material changes to existing credit facilities are reviewed and approved by the appropriate credit committee outlined below:

  1. Board Credit Committe
  2. Senior Credit Committee
  3. International Credit Committee
  4. Management Credit Committee (for small and medium-sized enterprises).

- The credit facility administration process is undertaken by a segregated function to ensure proper execution of all credit approvals and maintenance of documentation, and proactive control over maturities, expiry of limits, collateral valuation and contractual covenants.
- Country limits are determined based on the outlook of economic and political factors, along with the review of reports by rating agencies on the country (where available) and application of local business and market knowledge.
- Cross-border exposures are controlled by senior management in charge of relevant branches or subsidiaries and monitored by the central credit risk management function.

5.2.5 Key features of consumer credit risk management

- Credit risk management oversees the "consumer" segment through an independent unit directly reporting to Group Risk Management but working in partnership with the Consumer Banking business. Within this framework, limits and approval authorities are exercised by the officers with defined approval authorities.
- Consumer Credit Risk Management functional areas are aligned with key concepts of Risk Management, namely, Governance, Control, Measurement and Reporting.
- Consumer credit risk is managed with three lines of defence. As the first line of defence, the consumer business lending group (i.e. underwriting) is responsible for adherence to the credit policies, controls and processes. As second line of defence, the consumer risk management team, working independently of the business unit, assesses and ensures implementation of credit risk management discipline & policies. The third line of defence, the Internal Audit function, independently tests, verifies and evaluates controls for effective credit risk management & implementation of policies & procedures.
- All credit policies and amendments to policies are reviewed and approved annually by the Executive Committee and ratified by the Board.
- Credit risk "scorecard" models (such as Instalment Loan "Applicant" models) have been used to facilitate underwriting and monitoring of credit facilities to customers. Applicant "scoring" models are customer-centric models which incorporate CBK regulatory guidelines and Group policies related to consumer credit facilities, such as debt-to-income ratio, minimum qualifying income and limits on advances by product type. Additional inputs utilised include applicant characteristics obtained from credit bureaus, particularly Kuwait Credit Bureau statistics, to assist in assessing an applicant's ability to repay and the probability of default. This model is reviewed periodically for refinement.
- In 2008, the State of Kuwait established a Debt Relief Fund (i.e. DRF) dedicated to alleviate financial stress facing certain Kuwaiti Citizens. In that connection the Bank set up a special unit to assist customers who wished to participate in that process; for this DRF programme the application period ended March 2009 and applications were processed until 1st quarter 2011. The second Debt Relief Fund programme commenced on September 19th 2010 and applications were accepted until March 2011; final settlements of some of these cases are still pending. These official initiatives have been beneficial to customers concerned, who are better able to manage within their financial circumstance, and to the Bank in terms of reduced "past due" amounts.

5.2.6. Group credit risk monitoring

The Group's exposures are continuously monitored through a system of triggers and early-warning signals aimed at detecting adverse symptoms which could result in deterioration of credit risk quality. The triggers and early-warning systems are supplemented by facility utilisation and collateral valuation monitoring together with a review of upcoming credit facility expiration and market intelligence to enable timely corrective action by management. The results of the monitoring process are reflected in the internal rating process.

Credit risk is monitored on an ongoing basis with formal monthly and quarterly reporting to ensure senior management awareness of shifts in credit quality and portfolio performance along with changing external factors such as economic and business cycles.

Consumer credit risk reporting also includes a "dashboard" for consumer and small-business lending, classification and delinquency monitoring.

A specialised and focused problem loan "workout" team handles the management and collection of problem credit facilities.

5.2.7. Group credit risk mitigation strategy

Portfolio diversification is the cornerstone of the Group's credit risk mitigation strategy which is implemented through customer, industry and geographical limit structures.

To ensure diversification at the portfolio level, interrelated companies with the same management or ownership structure are classified and treated as one entity. The Group limits its credit concentration per entity to 15% of the Bank's regulatory capital.

Credit risk mitigants such as collateral and guarantees are effective mitigating factors within the Group's portfolio and collateral quality is continuously monitored and assessed. Risk transfer in the form of syndicated loans, risk participation arrangements with other banks and sale of loans are common practices to manage the Group's exposures.

5. RISK MANAGEMENT (Continued)

5.2.8 Management of credit collateral and valuation

The main types of collateral accepted by the Group are:

1. Cash collateral
2. Quoted shares
3. Bank guarantees
4. Commercial real estate
5. Sovereign debt instruments
6. Bank debt instruments
7. Collective investment schemes
8. Residential real estate.

In accordance with the Group's credit policies, banks and creditworthy companies and individuals with high net worth are accepted as guarantor counterparties, subject to credit risk assessment. Furthermore, in accordance with the CBK Basel II framework, only cash collateral, quoted shares, commercial real estate, debt instruments of sovereigns and banks and collective investment schemes are recognised as risk mitigation for capital adequacy purposes.

The custody and daily "mark to market" (revaluation) of financial collateral, inclusive of shares, are performed independent of the business units. Real estate collateral except private residences is valued on an annual basis.

The Group's credit exposures were covered by the following eligible financial collateral and guarantees:

KD 000's

	31 December 2012			31 December 2011		
	Gross credit exposure	Eligible Credit Risk Mitigation	Eligible guarantees	Gross credit exposure	Eligible Credit Risk Mitigation	Eligible guarantees
Cash	118,130	-	-	105,588	-	-
Claims on sovereigns	3,050,364	7	-	2,490,898	7	-
Claims on public sector entities	381,449	3,746	-	297,985	3,713	-
Claims on banks	2,847,315	2,310	641,519*	2,262,399	3,862	504,239*
Claims on corporates	8,299,385	2,640,116	-	7,155,864	2,284,664	-
Regulatory retail exposure	2,996,648	61,794	-	2,312,545	48,950	-
Past due exposures	150,533	83,068	-	72,561	-	-
Other exposures	728,240	-	-	498,211	-	-
Total	18,572,064	2,791,041	641,519	15,196,051	2,341,196	504,239

*"Memorandum" item where banks act as "guarantors"

5.2.9. Gross, average and net credit exposures

The Group's gross credit exposures, average credit exposures and the former adjusted for credit risk mitigation factors, respectively, are detailed below:

Gross credit exposures

KD 000's

	31 December 2012			31 December 2011		
	Gross credit exposure	Funded exposure	Unfunded exposure	Gross credit exposure	Funded exposure	Unfunded exposure
Cash	118,130	118,130	-	105,588	105,588	-
Claims on sovereigns	3,050,364	3,050,241	123	2,490,898	2,490,829	69
Claims on public sector entities	381,449	371,223	10,226	297,985	283,700	14,285
Claims on banks	2,847,315	2,010,166	837,149	2,262,399	1,579,771	682,628
Claims on corporates	8,299,385	6,610,722	1,688,663	7,155,864	5,746,241	1,409,623
Regulatory retail exposure	2,996,648	2,952,426	44,222	2,312,545	2,271,891	40,654
Past due exposures	150,533	150,533	-	72,561	72,561	-
Other exposures	728,240	728,240	-	498,211	498,211	-
Total	18,572,064	15,991,681	2,580,383	15,196,051	13,048,792	2,147,258

Average credit exposures

KD 000's

	31 December 2012			31 December 2011		
	*Average credit exposure	Funded exposure	Unfunded exposure	*Average credit exposure	Funded exposure	Unfunded exposure
Cash	111,584	111,584	-	104,446	104,446	-
Claims on sovereigns	3,059,374	3,059,261	113	2,832,232	2,832,176	56
Claims on public sector entities	358,721	345,788	12,933	265,942	228,016	37,926
Claims on banks	2,555,089	1,801,420	753,669	2,072,025	1,387,856	684,169
Claims on corporates	7,678,491	6,136,019	1,542,472	7,069,400	5,645,025	1,424,375
Regulatory retail exposure	2,642,361	2,597,127	45,234	2,263,366	2,214,136	49,230
Past due exposures	150,922	150,922	-	58,351	58,351	-
Other exposures	636,348	636,348	-	499,422	499,422	-
Total	17,192,890	14,838,469	2,354,421	15,165,185	12,969,429	2,195,756

* Based on monthly average balances

Risk Management Continued

5. RISK MANAGEMENT (Continued)

5.2.9. Gross, average and net credit exposures (continued)

Net credit exposures

KD 000's

	31 December 2012			31 December 2011		
	Net credit exposure	Funded exposure	Unfunded exposure	Net credit exposure	Funded exposure	Unfunded exposure
Cash	118,130	118,130	-	105,588	105,588	-
Claims on sovereigns	3,050,296	3,050,241	55	2,490,857	2,490,829	28
Claims on public sector entities	372,817	368,033	4,784	287,172	280,540	6,633
Claims on banks	2,416,369	2,007,963	408,406	1,903,995	1,575,909	328,086
Claims on corporates	4,828,599	4,013,511	815,087	4,142,171	3,489,012	653,159
Regulatory retail exposure	2,910,970	2,891,736	19,234	2,242,671	2,223,944	18,727
Past due exposures	67,465	67,465	-	72,561	72,561	-
Other exposures	728,240	728,240	-	498,211	498,211	-
Total	14,492,886	13,245,319	1,247,566	11,743,225	10,736,594	1,006,631

The Group uses external ratings (where available) from Fitch, S&P and Moody's to supplement internal ratings during the process of determining credit limits. Unrated public issue instruments are risk-weighted at 100% for capital adequacy purposes.

As at 31 December 2012, 34% (2011: 33%) of the Group's net credit risk exposure was rated by accredited External Credit Assessment Institutions (ECAIs), as detailed below:

KD 000's

	31 December 2012			31 December 2011		
	Net credit exposure	Rated exposure	Unrated exposure	Net credit exposure	Rated exposure	Unrated exposure
Cash	118,130	-	118,130	105,588	-	105,588
Claims on sovereigns	3,050,296	2,526,495	523,801	2,490,857	2,045,899	444,958
Claims on public sector entities	372,817	-	372,817	287,172	-	287,172
Claims on banks	2,416,369	2,233,315	183,054	1,903,995	1,658,460	245,534
Claims on corporates	4,828,599	214,704	4,613,895	4,142,171	152,261	3,989,910
Regulatory retail exposure	2,910,970	-	2,910,970	2,242,671	-	2,242,671
Past due exposures	67,465	-	67,465	72,561	-	72,561
Other exposures	728,240	-	728,240	498,211	-	498,211
Total	14,492,886	4,974,514	9,518,372	11,743,225	3,856,619	7,886,605

The geographical distribution of the gross credit exposure before taking into consideration credit enhancements is as detailed below:

KD 000's

31 December 2012	Middle East and North Africa	North America	Europe	Asia	Others	Total
Cash	94,363	1,095	22,672	-	-	118,130
Claims on sovereigns	2,434,241	531,162	64,649	20,312	-	3,050,364
Claims on public sector Entities	381,343	-	106	-	-	381,449
Claims on banks	1,630,249	76,141	542,918	565,360	32,647	2,847,315
Claims on corporates	7,409,491	257,699	432,419	100,449	99,327	8,299,385
Regulatory retail exposure	2,993,544	410	2,694	-	-	2,996,648
Past due exposures	148,640	-	1,351	542	-	150,533
Other exposures	551,311	39,541	78,353	46,039	12,996	728,240
Total	**15,643,182**	**906,048**	**1,145,162**	**732,702**	**144,970**	**18,572,064**

KD 000's

31 December 2011	Middle East and North Africa	North America	Europe	Asia	Others	Total
Cash	82,744	968	21,876	-	-	105,588
Claims on sovereigns	1,944,305	466,316	57,504	22,773	-	2,490,898
Claims on public sector entities	297,985	-	-	-	-	297,985
Claims on banks	1,254,991	72,353	363,634	536,849	34,571	2,262,399
Claims on corporates	6,447,445	186,667	354,151	129,062	38,539	7,155,864
Regulatory retail exposure	2,311,330	255	960	-	-	2,312,545
Past due exposures	70,795	-	-	1,766	-	72,561
Other exposures	411,913	38,230	31,744	12,715	3,609	498,211
Total	**12,821,509**	**764,789**	**829,869**	**703,165**	**76,719**	**15,196,051**

Risk Management Continued

5. RISK MANAGEMENT (Continued)

5.2.10. Maturity profile of gross credit exposure

The Group's gross credit exposure by residual contractual maturity is as detailed below:

KD 000's

31 December 2012	Up to 3 months	3 to 12 months	Over 1 year	Total
Cash	118,130	-	-	118,130
Claims on sovereigns	1,974,693	637,593	438,078	3,050,364
Claims on public sector entities	29,780	210,153	141,516	381,449
Claims on banks	1,771,481	317,141	758,693	2,847,315
Claims on corporates	4,242,204	2,092,756	1,964,425	8,299,385
Regulatory retail exposure	159,485	261,038	2,576,125	2,996,648
Past due exposures	150,533	-	-	150,533
Other exposures	39,264	17,558	671,418	728,240
Total	**8,485,570**	**3,536,239**	**6,550,255**	**18,572,064**

KD 000's

31 December 2011	Up to 3 months	3 to 12 months	Over 1 year	Total
Cash	105,588	-	-	105,588
Claims on sovereigns	1,642,263	510,248	338,387	2,490,898
Claims on public sector entities	7,517	121,432	169,036	297,985
Claims on banks	1,362,538	328,942	570,919	2,262,399
Claims on corporates	3,172,312	1,912,879	2,070,673	7,155,864
Regulatory retail exposure	153,345	257,562	1,901,638	2,312,545
Past due exposures	72,561	-	-	72,561
Other exposures	107,341	19,920	370,950	498,211
Total	**6,623,465**	**3,150,983**	**5,421,603**	**15,196,051**

5.2.11. "Past-due" and impairment provisions

Credit facilities are classified as "past-due" when a payment has not been received on its contractual payment date, or if the facility is in excess of pre-approved limits.

A credit facility is considered as "past-due and impaired" if the interest/profit or a principal instalment is past due for more than 90 days, or if the carrying amount of the facility is greater than its estimated recoverable value.

"Past due" and "Past-due and impaired" facilities are managed and monitored as "irregular facilities" and are classified into the following four categories which are then used to guide the provisioning process:

Category	Criteria
Watchlist	Irregular for a period up to 90 days (inclusive)
Substandard	Irregular for a period between 91 and 180 days (inclusive)
Doubtful	Irregular for a period between 181 days and 365 days (inclusive)
Bad	Irregular for a period exceeding 365 days

The Group may also include a credit facility in one of the above categories based on management's judgement of a customer's financial and/or non-financial circumstances.

The Group's impaired loan portfolio as at 31 December 2012 was KD 283,506 thousand (2011: KD 131,599 thousand) against which a specific provision of KD 151,047 thousand (2011: KD 107,390 thousand) has been made, as detailed below:

KD 000's

31 December 2012	Past due and impaired financing	Related Specific provision	Specific provision written off, net of exchange movement
Claims on sovereigns	51	51	-
Claims on banks	5,638	2,819	-
Claims on corporates	213,101	97,115	(47,895)
Regulatory retail exposure	64,716	51,062	(8,528)
Total	**283,506**	**151,047**	**(56,423)**

KD 000's

31 December 2011	Past due and impaired financing	Related Specific provision	Specific provision written off, net of exchange movement
Claims on sovereigns	61	61	-
Claims on banks	-	-	(697)
Claims on corporates	68,583	57,284	(10,840)
Regulatory retail exposure	62,955	50,045	(135)
Total	**131,599**	**107,390**	**(11,672)**

The geographical distribution of "past-due and impaired "financing and the related specific provision is as follows:

KD 000's

31 December 2012	Middle East and North Africa	Europe	Asia	Others	Total
Past due and impaired financing	283,498	3	-	5	283,506
Specific provision	**151,040**	**2**	**-**	**5**	**151,047**

KD 000's

31 December 2011	Middle East and North Africa	Europe	Asia	Others	Total
Past due and impaired financing	128,794	14	2,786	5	131,599
Specific provision	**105,910**	**12**	**1,463**	**5**	**107,390**

5. RISK MANAGEMENT (Continued)

5.2.11. "Past-due" and impairment provisions (Continued)

In accordance with CBK regulations, a general provision of 1% for cash facilities and 0.5% for non-cash facilities (2011: 1% for cash facilities and 0.5% for non-cash facilities) is made on all applicable credit facilities (net of certain restricted categories of collateral) which are not subject to specific provisioning.

The adequacy of provisions are regularly evaluated and monitored by the Credit Provisions Committee.
The Group's total provision as at 31 December 2012 was KD 457,637 thousand (2011: KD 343,288 thousand) inclusive of a general provision of KD 278,572 thousand (2011: KD 198,590 thousand) as detailed below:

31 December 2012	KD 000's General provision
Claims on sovereigns	199
Claims on banks	3,981
Claims on corporates	237,742
Regulatory retail exposure	36,650
Total	**278,572**

31 December 2011	KD 000's General provision
Claims on sovereigns	197
Claims on banks	1,561
Claims on corporates	166,081
Regulatory retail exposure	30,751
Total	**198,590**

The total general provision above includes KD 23,844 thousand (2011: KD 22,008 thousand) relating to "non-cash" facilities in accordance with CBK regulations.

The geographical distribution of the general provision on "cash" facilities is as follows:

KD 000's

31 December 2012	Middle East and North Africa	North America	Europe	Asia	Others	Total
General provision	248,646	1,394	3,265	373	1,050	**254,728**

KD 000's

31 December 2011	Middle East and North Africa	North America	Europe	Asia	Others	Total
General provision	171,456	1,176	2,835	714	401	**176,582**

The analysis of specific and general provisions is further detailed in note 11 of the Group's consolidated financial statements.

5.3 "Market" risk

"Market" risk is defined as the potential loss in value of financial instruments caused by adverse movements in market variables such as interest rates, foreign exchange rates and equity prices.

Market risk results from uncertainty in future earnings arising from changes in interest rates, exchange rates, market prices and volatilities.

The Group assumes market risk from financial claims and loans, position-taking, and trading and investment activities.

The strategy for controlling market risk involves:

- Stringent controls and limits.
- Strict segregation of "front" and "back" office duties.
- Regular reporting of positions.
- Regular independent review of all controls and limits.
- Rigorous testing of pricing, trading and risk management systems.

5.3.1. Market-risk management framework

The market-risk management framework governs the Group's trading and non-trading related market risk. Market risk stemming from trading activities is managed by the Group Treasurer. The management and oversight of market risk inherent within the Group's non-trading activities is the primary responsibility of the Group Asset and Liability Executive Committee, supported by the regional Asset and Liability Committees. All activities giving rise to market risk are conducted within a structure of approved credit and position limits.

5.3.2. Monitoring of "market" risk from "trading" activities

The Group risk management function independently monitors the regional and global trading market risk exposure through a Value-at-Risk methodology (VaR) to derive quantitative measures specifically for market risk under normal market conditions. This enables the Group to apply a constant and uniform measure across all of its trading activities and facilitates comparisons of market risk estimates, both over time and against daily trading results. VaR is calculated using a 99% "confidence level" and a holding period of ten days in line with Basel Committee guidelines.

On a daily basis, VaR is supplemented with stress-testing to quantify market risk under extreme stress scenarios based on observed historical worst-case and in-house developed scenarios. VaR computation allows for diversification benefits at the Group level. Furthermore, the Group recognises and mitigates the correlation of other risks and processes on its market-risk monitoring process. In addition to VaR, the Group uses a structure of limits to manage and control its market risk associated with trading activities. The Group also produces stressed VAR using the same framework. Computations are based on stressed historical data.

5.3.3. Monitoring of exposures under interest-rate swap transactions

The Group risk management function independently monitors risk exposures under "interest-rate swap" transactions using the concept of Potential Future Exposure. Potential Future Exposure (PFE) is defined as the maximum exposures over a specified period of time calculated at 99% confidence level. As such, the risk is an upper bound at the selected confidence interval for future exposure and not the maximum risk exposure possible.

5.3.4. Monitoring of non-trading market risk in the banking book

The Group's key non-trading market risk is the sensitivity of its net interest income to movements in interest rates.

The interest-rate risk in the "banking book" is managed through a "gap" limit structure which is supplemented by periodic analysis of scenarios (instantaneous parallel shift of +/-5 bps and +/-10bps to the yield curve) to capture the extreme indicative measure of exposure to interest rate changes. The analysis of scenarios showed an impact in the banking book as follows:

KD 000's

31 December 2012	+ 5bp	-5bp	+10bp	-10bp
	808	(808)	1,616	(1,616)

KD 000's

31 December 2011	+ 5bp	-5bp	+10bp	-10bp
	1,069	(1,069)	2,138	(2,138)

5. RISK MANAGEMENT (Continued)

5.3.4. Monitoring of non-trading market risk in the banking book (Continued)

The Group does not use the result of scenario analysis to predict changes in its earnings because of the simplified assumptions inherent in the scenario analysis. Such assumptions includes that interest rates move by the same percentage irrespective of maturity, that all positions run to maturity and that no management corrective action is taken to mitigate the impact of interest-rate risk. In addition to interest rate risk, the Group is also exposed to market risk as a result of changes in the "fair value" of its strategic equity and investment positions held without any intention of liquidation.

The Group's total equity investment portfolio as at 31 December 2012 was KD 136,912 thousand (2011: KD 73,303 thousand), 24% (2011: 52.0%) of which related to quoted investments. The cumulative realised gains arising from sale of equity investments during 2012 were KD 4,964 thousand (2011: KD 149 thousand).

All revaluation gains or losses during the year relating to equity investments were recorded in the consolidated statement of financial position. The cumulative net unrealised gain for equity investments recognised in the consolidated statement of financial position were KD 15,089 thousand (2011 : KD 16,780 thousand) of which KD 6,790 thousand (2011: KD 7,551 thousand) is included in Tier 2 capital of the Group. For additional details of the accounting policies related to the valuation of equity holdings, refer to notes 2.19 and 2.20 of the Group's consolidated financial statements.

5.4. Operational risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events.

5.4.1. Operational-risk management framework

The Group monitors its operational risks on a regional and global basis through an operational-risk management framework which defines roles and responsibilities for managing and reporting operational risk. The key components of this framework are comprehensive documented policies, procedures and internal controls.

Through the framework, line management is able to identify, assess and decide in what form and scale it can accept, control and reduce operational risk, together with the form of risk-prevention measures which are necessary. Furthermore, it embeds a culture of transparency of information, escalation of key issues and accountability for issue resolution. Group risk management collates and reviews actual and potential loss data arising from the Group's day-to-day operations to continuously refine its control arrangements.

The operational-risk framework is supplemented by regular reviews from the Group internal audit function. The Group has a business continuity plan together with a fully-equipped disaster recovery centre which is tested periodically.

The Group's business processes are closely monitored to identify, assess, control and prevent potentially illicit use of the Group's services for laundering money and/or financing terrorism. The Group's "anti-money laundering" and "combating terrorism-financing" initiatives are regularly reviewed to ensure full compliance with local legal and regulatory requirements and international best practices.

5.5. Liquidity risk

Liquidity risk is defined as the inability to generate sufficient financial resources to meet all obligations and commitments as they fall due, or having to access funds to meet payment obligations at an excessive cost. It is the policy of the Group to maintain adequate liquidity at all times, in all geographical locations.

The Group applies a prudent mix of liquidity controls which provide security of access to funds without undue exposure to increased costs of funds from the liquidation of assets, or aggressive bidding for deposits. Liquidity risk is monitored and evaluated daily to ensure that, over the short term and by major currency, the profile of projected future cash inflows is adequately matched to the maturity of the liabilities.

5.6. Reputation and fiduciary risk

Reputation risk is defined as the current and prospective impact on earnings and capital arising from negative public opinion that will impact the ability to establish new relationships or services or to continue servicing existing relationships.

Management of reputation risk is an inherent feature of the Group's corporate culture which is embedded as an integral part of the internal control systems. Besides identification and management of risks, the internal control system also incorporates as an ethos the maintenance of business practices of the highest quality towards its customers, shareholders, regulators, general public and fiduciary and non-fiduciary clients.

Through its policies and practices NBK ensures that proper screening of clients' risk profiles and performance expectations is conducted prior to making investment products or services available to them. Furthermore, once a product or service is sold, appropriate risk and performance projections are clearly communicated, and funds placed under management are treated with due care and professionalism.

During the year, Assets under Management at the Group increased by 11.3% to reach KD 2,817 million on 31 December 2012 (2011: KD 2,530 million).